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Magalie Roman Salas Secretary Federal Communications Commission 1919 M St., N.W. Washington, D.C. 20554

> Re: Deployment of Wireline Services Offering Advanced Telecommunications Capability, CC Docket No. 98-147

Dear Ms. Salas:

On behalf of Qwest Communications Corporation ("Qwest"), enclosed for inclusion in the record of the referenced proceeding are (1) a copy of "CLEC Access to xDSL Technology: A Necessary Predicate for Widespread, Competitive Deployment of Broadband Telecommunications Services," LCI International Telecom Corp. White Paper, dated June 1998; and (2) a copy of the "Petition of LCI International Telecom Corp. for Expedited Declaratory Rulings, A 'Fast Track' Plan To Expedite Residential Local Competition And Section 271 Entry Through Establishment Of Independent RBOC Wholesale And Retail Service Companies," dated January 22, 1998. These documents were referenced in Qwest's initial comments, filed September 25, 1998, in the referenced docket.

Please contact me if you have any questions.

Respectfully submitted,

Lindh Lolling

Linda L. Oliver

Counsel for Qwest Communications

Corporation

**Enclosures** 

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### CLEC Access to xDSL Technology:

### A Necessary Predicate for Widespread, Competitive Deployment of Broadband Telecommunications Services

### LCI International Telecom Corp.

June 1998

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#### EXECUTIVE SUMMARY

The technology is now available to enable customers -- in particular, residential and small business customers -- to obtain high-speed access to corporate networks and the Internet over the same twisted pair of copper wires that now provides them with telephone service and relatively low speed Internet access. The potential of such technology -- generically referred to as "digital subscriber line" or "xDSL" -- is great. For that potential to be fully realized, however, it is essential that the local market-opening provisions of the Communications Act continue to apply as the local exchange network evolves to a broadband capability.

#### The Section 706 Petitions

Three regional Bell operating companies (RBOCs) have asked the Federal Communications Commission to forbear from applying the unbundled network element and resale provisions of the Communications Act to their investments in xDSL technology. They argue that such forbearance is necessary to provide them the appropriate incentives to invest in such network improvements, even though each of them is already making such investments. The Association for Local Telecommunications Services (ALTS) also has filed a petition under Section 706, asking the FCC to make clear that the Act's market-opening provisions make no distinctions on the basis of the nature of technology used, or whether the local network is used to provide voice or data services.

As this White Paper shows, the ability of consumers to reap the fruits of competition in the local exchange, and to have a choice of providers of broadband telecommunications services (as well as Internet service providers), will depend on the ability of competitors to access the xDSL capabilities in the ILEC network.

#### xDSL as the Next Step in the Evolution of Technology that Boosts Network Capability

All of the RBOCs and GTE have announced the commercial roll-out of xDSL-based services for small business and residential customers. This technology represents the next step in a natural evolution of improvements that boost the capability and speed of the existing network. Over time, telecommunications networks have moved from analog to digital transmission, from in-band to out-of-band signaling (SS7), from copper to fiber optic facilities, and from circuit-switched to packet-switched transmission systems. xDSL is just another step in this natural progression. It involves the use of electronics on the existing copper wires to increase the capacity of those wires -- just as ISDN services and T-1 lines (using HDSL electronics) have been provided.

#### Three Entry Strategies

The Communications Act makes available three paths for entry into the local exchange market: (1) competition by construction of new local facilities and interconnecting with the incumbent; (2) lease of the ILEC's network elements (in whole or in part) to provide competing service; and (3) resale of the ILEC's retail services at a wholesale rate. The RBOC petitions attempt to deny competitors the ability to employ the second and third strategies when it comes to xDSL capability.

Requiring competitive local exchange carriers (CLECs) to provide their own xDSL electronics and to collocate at central offices if they wish to provide xDSL services contradicts the letter and purpose of the Act. The Act allows neither regulators nor ILECs to decide when and where it is cost-effective to construct facilities in lieu of using ILEC network elements. By allowing new entrants to take full advantage of incumbent LECs' scale and scope economies, the Act enables competition to proceed more rapidly and to reach more broadly, to include customers that cannot be economically served by competitors if they must construct new facilities.

#### No Legal Basis to Fence Off xDSL Technology

The Act's forbearance provisions do not permit the FCC to forbear from applying the unbundling and resale provisions of Section 251(c) until that section is "fully implemented." The Commission therefore lacks authority to forbear. Section 706, upon which the RBOCs rely, does not confer additional forbearance authority on the FCC. Rather, Section 706 simply encourages the FCC and state commissions to use any of a number of tools they already possess to encourage the spread of advanced technologies. One of those tools, in fact, is the promotion of local competition -- a goal that would be thwarted by grant of the RBOCs' petitions.

In seeking forbearance, the RBOCs implicitly concede that the Section 251(c) unbundling and resale obligations apply to xDSL technology, and properly so.

The Act's definition of "network element" is broad, and includes all "features, functions, and capabilities" of a "facility or equipment used in the provision of a telecommunications service." 47 U.S.C. § 153(29). Nothing in the definition of network element or in the Act limits this provision to existing technology, to voice services, or to circuit-switching technology.

Loops equipped with xDSL electronics, and the local switching and transport associated with xDSL transmissions, are squarely within the definition of a network element. It would be incorrect to define a loop without regard to the electronics attached to the loop, which make the loop capable of transmission. The deployment of digital loop carrier (DLC) electronics in remote terminals is but one example of the integral role of electronics in enabling the loop to function.

#### The High Costs Facing Competitors to Deploy Duplicate xDSL Technology

In their petitions, the RBOCs claim to need extra incentives to deploy the large investment required to provide on a broad basis xDSL-based services. Yet they also claim that their competitors, who begin with virtually no local market share, should be required to make this same investment before serving a single customer, even though such competitors, by definition, do not have the volumes necessary to justify collocating DSLAM electronics in every central office and creating a duplicate, high capacity interoffice network that could haul the xDSL traffic back from every central office to the competitor's packet switch.

US West claims that it will not serve the less densely populated central offices without the extra incentive of being able to shield its investment in xDSL technology from competitors. But if US West can barely afford to serve those areas, it is clear that competitors, who can expect to gain much smaller volumes, will not economically be able to provide service in those areas (as well as in other more dense areas). The consequence of forcing competitors to install their own xDSL electronics, switching and local transport will be that few consumers will have a competitive choice of broadband telecommunications service providers.

Using the Dallas/Forth Worth LATA as an example, it becomes clear that with the typical charges now levied for physical collocation of DSLAM equipment, a new entrant the size of LCI could not economically serve the vast majority of central offices in that LATA. Even if physical collocation were made less expensive, or if alternatives to physical collocation were pursued, the result still is that many central offices are not likely to be served. Such calculations do not even take into account the huge cost disadvantages faced by entrants to duplicate the existing interoffice transport network of the ILEC, and does not consider the higher per-line costs faced by CLECs—including, for example, the cost of hiring and dispatching technicians; engineering the network; maintenance, repair, and remote testing; and coordinating with the ILEC for installation. It also does not consider the delay and cost of negotiating, arbitrating, and resolving disputes with the ILEC.

#### Consistency with the Future

Providing CLECs with access to xDSL technology also should help to ensure a competitive environment for Internet Service Providers (ISPs), because they would not face a potentially monopolistic provider of broadband telecommunications services. As pointed out by the Commercial Internet Exchange Association, the market-opening provisions of the Act are critical to ensuring the healthy development of a competitive market for ISPs.

It also would be both legally and technically unsustainable to attempt to create a more liberal regulatory regime for packet-switched networks and data services. The Act does not make such distinctions, and it is likely that voice will eventually be provided over broadband data networks. Regulators should refrain from drawing lines on the basis of technology and cost assumptions that will necessarily become obsolete as technologies develop and cost characteristics change.

#### No Added Incentives Needed

The RBOCs do not need the added incentive of deregulated treatment of advances in technology. All the RBOCs and GTE have announced major commercial rollouts of xDSL based services, and will likely continue to expand such efforts. Deregulated treatment would mean, instead, that the ILECs would extend their current dominance in the local exchange into the future.

Enforcing the Act's market-opening provisions equally for all technologies and services is the best way to ensure wide deployment of advanced technology and the broad availability of competitive choices in advanced telecommunications services for all consumers.

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#### INTRODUCTION

A number of RBOCs have asked the Federal Communications

Commission (FCC) to forbear from requiring them to make available to their

competitors the advanced capabilities of their incumbent local exchange networks.

In particular, they seek to shield from competitors access to "xDSL" technology,

which increases the capacity and speed of existing copper subscriber loops. 1/ These

RBOCs (Bell Atlantic, US West, and Ameritech) rely on Section 706 of the 1996

Telecommunications Act, which prompts the FCC to take appropriate action to

encourage the broad deployment of advanced technology, and requires it to conduct

an inquiry this summer into that subject. 2/

The Association for Local Telecommunications Services (ALTS) also recently filed a petition under Section 706.3/ In that petition, ALTS urges the

<sup>1/</sup> Petition of Bell Atlantic for Relief from Barriers to Deployment of Advanced Telecommunications Services, filed January 26, 1998, CC Docket No. 98-11; Petition of US West Communications, Inc. for Relief from Barriers to Deployment of Advanced Telecommunications Services, filed February 25, 1998, FCC Docket No. 98-26; Petition of Ameritech Corporation to Remove Barriers to Investment in Advanced Telecommunications Capability, filed March 5, 1998, CC Docket No. 98-32.

<sup>2/ 47</sup> U.S.C. § 157(note). In this paper, we limit our discussion to the availability of xDSL technology to competitors, and do not address the RBOCs' requests for interLATA relief for their data services or their other requests for forbearance from important regulatory requirements.

<sup>3/</sup> Petition of the Association for Local Telecommunications Services for Declaratory Ruling Establishing Conditions Necessary to Promote Deployment of Advanced Telecommunications Capability Under Section 706 of the Telecommunications Act of 1996, filed May 27, 1998, with the Federal Communications Commission.

Commission to make clear that the Communications Act requires the incumbent local exchange carriers ("ILECs") to open their local networks for competition in the provision of *all* telecommunications services, whether data or voice, and regardless of the technology used. Such competition, ALTS correctly points out, is what will form the basis for competition and consumer choice in broadband telecommunications services.

In their petitions, in contrast, the RBOCs contend that the only way to create incentives for them to develop technologically advanced networks is to permit them to fence off network improvements from competitors and to relieve the RBOCs of regulatory requirements that are intended to protect the public from their exercise of market power. In essence, these RBOCs ask the Commission to allow them to evade the critical local competition provisions of the Act by freezing the local exchange network in time, relegating competitors to use of inferior technology, depriving competitors of the ability to compete as the network evolves, and robbing consumers of the chance to enjoy the benefits of competition in broadband-network-based services. 4/

<sup>4/</sup> Under the RBOCs' plans, they would be free to: (1) offer new or advanced services without providing other carriers access to the underlying facilities needed to provide those services, contrary to the pro-competitive unbundling requirements of Section 251(c)(3); (2) deny competitors the ability to resell those services pursuant to Section 251(c)(4); (3) construct and use interLATA transmission facilities without first complying with the local market-opening requirements of Section 271, and (4) engage in these activities without the protections of the structural separation requirements of Section 272. 47 U.S.C. §§ 251(c)(3), 251(c)(4), 271, 272.

Consumer choice of broadband service providers, and competitive pricing of those services, will depend completely on the ability of competitors to access the xDSL capabilities in the ILEC networks. Residential customers and small businesses, in particular, will be harmed if the network unbundling and resale requirements do not apply to advanced services. Section 706 itself contemplates that local competition is one important mechanism for delivering advanced services more quickly and more broadly. 5/ Grant of any part of the RBOCs' petitions would chill the development of that competition in broadband telecommunications services, leaving most small businesses and consumers with no choice of broadband service providers.

# I. CONSUMER CHOICE OF BROADBAND PROVIDERS DEPENDS ON COMPETITIVE ACCESS TO XDSL CAPABILITIES IN THE ILEC NETWORK.

#### A. The Consumer Potential of xDSL Technology

Customers, particularly residential and small-business customers, increasingly are demanding the delivery of high speed, digital, broadband telecommunications services. The use of Digital Subscriber Line ("DSL" or "xDSL") electronics with existing copper (or copper and fiber) loops can help to meet this demand in a cost-effective manner. 6/

<sup>5/</sup> Section 706 requires the Commission to use "measures that promote competition in the local telecommunications market" as one means to stimulate deployment of advanced technology. 47 U.S.C. § 157 note.

<sup>6/</sup> Put simply, "DSL" or "xDSL" is a technology that employs electronics to boost the capacity, speed, and capability of existing telephone lines. In Appendix A we set

For the majority of small-business and residential customers, the limited capacity of the copper local loop has been the single most important obstacle to their access to broadband telecommunications services. Since the mid-1990s, the increasing deployment of xDSL electronics has made possible the delivery of broadband telecommunications services at a cost that is within the reach of most small businesses and many consumers. Over xDSL-equipped loops, 7/ these consumers can enjoy high-speed access (in the megabits per second range) to the Internet or to corporate networks, instead of the hypothetical top speeds of 56 kilobits per second provided by voice-grade modems. BellSouth estimates, for example, that its ADSL service can provide speeds of up to 50 times that of conventional modems. 8/

forth the different forms of xDSL and their characteristics. Appendix B is a diagram of xDSL technology deployed in a "home run copper" installation (where a copper pair runs from the customer premises all the way to the central office). Appendix C is a diagram of xDSL technology deployed in a remote "digital loop carrier" (remote DLC) installation. In a DLC installation, the copper pair runs from the customer premise to a remote DLC terminal, where it is multiplexed with other lines onto fiber (or sometimes copper) facilities that run directly into the ILEC central office switching facilities. In Appendix D we set forth in detail a description of xDSL technology and how it works, both for home run copper and DLC installations.

If By "xDSL-equipped loop" we mean the transmission facility from the customer premises to the switch -- i.e. the xDSL modem, the copper wire or fiber, the DSLAM, and (for loops connected to the switch by a DLC) the DLC (including the line cards and FOTS).

<sup>8/</sup> News Release, "BellSouth Announces Aggressive 30 Market Roll-Out of Ultra-High Speed BellSouth.Net FastAccess ADSL Internet Services," May 20, 1998, at www.bellsouthcorp.com.

The increased use of xDSL-equipped loops also reflects the increasing importance of data telecommunications relative to voice. Internet traffic is growing at 1,000% a year and data traffic over the public switched network is doubling annually. 9/ By contrast, voice traffic is expanding at only single-digit rates. 10/ Data traffic already accounts for over half the total traffic of most U.S. carriers. One analyst estimates that by the year 2005, the volume of data traffic is expected to be 23 times the volume of voice traffic. 11/

xDSL electronics can help accommodate a large share of the data demand from small businesses and consumers without much additional investment in network infrastructure. It leverages investments that incumbent local exchange carriers ("ILECs") already have made (in twisted copper pair, Digital Loop Carrier electronics in the field, and fiber feeders in the local distribution plant), enabling the existing local exchange network to support higher-bandwidth telecommunications services to a far greater number of customers. xDSL thus can form the basis for the expansion of consumer choice into the broadband world -- but only if the ILECs' investments in xDSL remain subject to the local competition provisions of the Communications Act.

<sup>9/ &</sup>quot;Lucent Agrees to Buy Yurie for \$1 Billion" Wall Street Journal, April 28, 1998.

<sup>10/</sup> Id.

<sup>11/</sup> Id., quoting Christopher Stix of Cowen & Co.

## B. xDSL is a Manifestation of the Natural Evolution of the Network to Higher Speeds and Greater Digital Capabilities.

xDSL is only the most recent manifestation of the natural evolution of the telephone network to increased digital capabilities and higher speed transmission. Over time, telecommunications networks have moved from analog to digital transmission, from in-band to out-of-band signaling (SS7), from copper to fiber optic facilities, from circuit-switched to packet-based transmission systems, and so on. xDSL technology is just another step in this natural progression.

xDSL also is just another example of the use of electronics in the network to boost the capabilities and the capacity of the existing infrastructure. For example, multiplexers deployed in the ILEC network can multiply by many factors the speed of traffic over the same copper or fiber-optic strand. ISDN technology deployed at either end of a copper loop (or at the remote digital loop carrier, in the case of DLC installations) can create digital capability, additional lines, and higher speed on that existing copper facility. xDSL is no different.

xDSL also does not require the use of radically new functionalities.

Indeed, ILECs have used xDSL electronics for over five years to maximize the efficiency of their networks. For example, ILECs have used a version of xDSL known as HDSL to support high bandwidth (T-1) transport for both end users and carrier-customers. 12/ Those T-1 lines can be used by customers for both voice and

<sup>12/</sup> A channelized T-1 service is the equivalent of 24 64 kbps (voice-grade equivalent) channels and operates at 1.544 Mbps speeds.

data transmissions at high capacity. In a similar manner, placement of xDSL electronics in the local loop allows subscribers to place voice calls over the circuit-switched network and to access data networks simultaneously over a single line, and to obtain high speed access to data networks.

In sum, although the ILECs attempt to paint xDSL technology as somehow different (and thus off-limits to competitors), in fact xDSL is another in a long line of advances in network technology -- advances that are sure to continue, and sure to evolve in as-yet unanticipated ways.

# II. IT IS ESSENTIAL TO PRESERVE THE THREE ENTRY STRATEGIES GUARANTEED BY CONGRESS AS THE INCUMBENT LEC NETWORK EVOLVES.

The Communications Act 13/ specifically makes available three entry strategies to CLECs that wish to provide competing local telecommunications services. First, a competitor may provide such services entirely over its own facilities. Congress recognized that even such facilities-based CLECs would require access to the ILEC networks in most cases and, therefore, required ILECs to provide nondiscriminatory interconnection to their networks. See 47 U.S.C. § 251(c)(2). Second, a CLEC may enter the market for local telecommunications services through the use of unbundled network elements (either all or some of the elements required to provide the service). See 47 U.S.C. § 251(c)(3). Finally,

<sup>13/</sup> Communications Act of 1934, as amended, 47 U.S.C. § 151 et seq. (hereafter "the Act")

CLECs may resell retail local telecommunications services purchased from ILECs at wholesale rates. See 47 U.S.C. § 251(c)(4).

The Communications Act does not express any preference among these three service delivery methods. It provides flexibility to CLECs in order to encourage speedy and broad-based competition in all market segments and for all services. Congress recognized that facilities-based competition may not materialize everywhere, serve everyone, and provide competitive choices for all services and, therefore, provided CLECs with the right to employ the ILEC network infrastructure (as network elements) in order to hasten the arrival and reach of local competition. 14/

Requiring CLECs in all cases to provide their own xDSL electronics and to collocate at central offices if they wish to provide xDSL services contradicts Congressional intent and the plain language of the Act by forcing CLECs to install equipment of their own as a precondition to provision of xDSL services. 15/ As the

<sup>14</sup> See, e.g., Joint Statement of Managers, S. Conf. Rep. No. 104-230, 104th Cong., 2d Sess. at 148 (1996) ("This Conference Agreement recognizes that it is unlikely that competitors will have a fully redundant network in place when they initially offer local service, because the investment necessary is so significant. Some facilities and capabilities (e.g., central office switching) will need to be obtained from the incumbent local exchange carrier as network elements pursuant to new Section 251").

<sup>15/</sup> Any facilities requirement, whether physical collocation, virtual collocation, cageless collocation, or otherwise, will have the same chilling effect on competitive deployment of broadband telecommunications services, because each of these methods requires having a physical presence in the central office -- with its associated up-front costs, economies of scale, and installation/maintenance/remote testing issues. These methods would also require huge investment in interoffice

Eighth Circuit Court of Appeals has made clear, a carrier need not own any of its own facilities in order to provide telecommunications services over network elements purchased from the ILEC. 16/Such a facilities requirement would also have the effect of restricting and discouraging broadscale deployment of xDSL services by CLECs. It would mean, as a practical matter, that CLECs can profitably supply xDSL services only to customers concentrated in dense commercial areas or served by central offices with a large number of potential customers. 17/

The Act allows neither regulators nor ILECs to decide when and where it is cost-effective to construct facilities in lieu of the CLEC being given access to unbundled network elements. Congress left that choice to the CLEC. Moreover, as the FCC concluded, requiring facilities investment as a condition to competing in the local market would inhibit the development of local competition. The Commission specifically rejected the argument that forcing requesting carriers to own some of their own facilities would somehow spur local exchange competition. Instead, the FCC concluded that "such a result could diminish competition, and that allowing new entrants to take full advantage of incumbent LECs' scale and

dedicated transport and packet switching, unless these capabilities can be obtained as network elements, including the availability of shared transport.

<sup>16/ &</sup>lt;u>Iowa Utilities Board v. FCC</u>, 120 F.3d 753, 814 (8th Cir. 1997), <u>cert. granted</u>, 118 S. Ct. 879 (1998).

<sup>17/</sup> We discuss in Section IV below why competitors cannot economically provide their own xDSL electronics and interoffice facilities on a broad basis.

scope economies will promote more rapid and efficient entry and will result in more robust competition." 18/

### III. THERE IS NO LEGAL BASIS FOR FENCING OFF XDSL TECHNOLOGY.

### A. The BOCs Improperly Rely on Section 706 to Shield Them From Their Statutory Obligations.

Several RBOCs have asked the FCC to forbear from requiring them to make available to their competitors the advanced capabilities of their incumbent local exchange networks. These large ILECs would like the FCC to allow them to escape their statutory obligations to make their advanced network capabilities available to competitors as "network elements" pursuant to Section 251(c)(3) of the Communications Act and to resell their advanced retail services at wholesale rates under Section 251(c)(4) of the Act. 19/

In seeking forbearance, these RBOCs implicitly acknowledge these statutory obligations. They also appear to recognize that the Act's forbearance provision (Section 10) does not permit the FCC even to consider forbearing from

<sup>18/</sup> In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499 (1996), aff'd in part and rev'd in part, Iowa Utilities Board v. FCC, 120 F.3d 753 (8th Cir.), cert. granted, 118 S. Ct. 879 (1998) ("Local Competition Order") at para. 340 (emphasis added).

<sup>19/</sup> As discussed in note 2, above, this paper does not address the other RBOC forbearance requests.

Section 251(c) requirements until that section is "fully implemented." 20/ The RBOCs seek forbearance not under that general statutory forbearance provision, but instead under Section 706 of the Telecommunications Act, 47 U.S.C. § 157(note). 21/ However, Section 706 is a broad instruction to both the FCC and the state commissions to use whatever authority they have to promote advanced technology deployment; it does not constitute an independent grant of authority to either the FCC or the states.

The RBOC petitions also ignore the fact that Section 706 itself contemplates that the FCC will use the promotion of local competition as a means for encouraging the deployment of advanced technology. The RBOCs' petitions would have the FCC do the polar opposite: allow them to *impede* local competition as a means to advance the deployment of advanced technology. This is clearly not what Congress had in mind.

The FCC will be conducting the required inquiry under Section 706 later this summer, and will doubtless explore many proposals to promote

<sup>20/ 47</sup> U.S.C. § 160 Sections 10 and 332(c) contain the only generic forbearance authority in the Communications Act. See 47 U.S.C. § 160, 332(c). Section 10(d) contains the "fully implemented" restriction, and Section 332(c) only applies to commercial mobile radio (i.e. wireless) services.

<sup>&</sup>lt;u>21</u>/ Section 706 requires the FCC and each state commission to take steps to promote "reasonable and timely" advanced technology deployment "by utilizing, in a manner consistent with the public interest, convenience, and necessity, price cap regulation, regulatory forbearance, measures that promote competition in the local telecommunications market, or other regulating methods that remove barriers to infrastructure investment." 47 U.S.C. § 157(note).

deployment of advanced technology. LCI enthusiastically supports the goals of Section 706. The point of this white paper, in fact, is to show that the goals of Section 706 will be best achieved if advances in the ILEC network are available to all competitors, and not only to the incumbent LEC. It should go without saying that if the ILEC can relegate competitors to using only the old capabilities of the network, while reserving to themselves the new capabilities, that consumers will not reap the benefits of competition as technology advances, but rather will revert to having only one choice -- the monopoly local exchange carrier.

## B. The Act Does Not Limit Competitors' Access to ILEC Network Capabilities.

While the RBOC petitions do not contest their obligations to make xDSL technology available to competitors under Sections 251(c)(3) and 251(c)(4), we nevertheless discuss in this section the legal underpinnings of the right of competitors to access the ILECs' xDSL capabilities without owning or installing their own facilities.

The efforts of incumbent LECs to limit CLEC access to specific equipment or capabilities in the ILEC network is flatly contrary to the Act. Section 3 of the Act defines "network element" broadly to include all "features, functions, and capabilities" of a "facility or equipment used in the provision of a telecommunications service." 47 U.S.C. § 153(29). xDSL functionality falls squarely within this definition. Nothing in the definition of network element or the Section 251(c) unbundling provisions would suggest that the availability of the

"features, functions, and capabilities" of ILEC network facilities or equipment is limited to voice services or to circuit-switching technology. The plain language of Section 251(c)(4) also requires the ILEC to permit CLECs to resell ILEC xDSL-based retail services at wholesale rates. 47 U.S.C. § 251(c)(4).

Indeed, the FCC underscored the importance of giving CLECs access to the network as the technology evolves. The FCC's <u>Local Competition Order</u> provides that the unbundling rules "must accommodate changes in technology." <u>22/</u> In a dynamic industry like telecommunications, competitors would be at a severe competitive disadvantage if they could not employ new capabilities of the ILEC network as it evolves. The Eighth Circuit also recognized that giving competitors broad access to ILEC network elements would on balance spur more innovation that denying such access: "the pro-competitive effects of unbundling... could spur enough innovation to offset any potential reduction in innovation that the unbundling standard might cause." <u>23/</u>

Requiring CLECs to install their own DSLAM equipment or their own packet switching and transport facilities in order to be able to compete in the provision of broadband telecommunications services also would violate the Act.

Requesting carriers have the right to purchase and combine all the network elements required to provide service, without owning any of their own facilities. 24/

<sup>22/</sup> Local Competition Order at para. 259

<sup>23/</sup> Iowa Utilities Board v. FCC, 120 F.3d 753 at 811.

<sup>24/</sup> Local Competition Order at paras. 328-40.

The Eighth Circuit affirmed the FCC on this point, holding that "a competing carrier may obtain the ability to provide telecommunications services *entirely through* an incumbent LEC's unbundled network elements..." 25/

Whether a requesting carrier is able to duplicate any particular network element or capability is irrelevant to that carrier's right to obtain it, instead, from the ILEC. On the contrary, the FCC found in its August 1996 Local Competition Order that "[r]equiring new entrants to duplicate unnecessarily even a part of the incumbent's network could generate delay and higher costs for new entrants...," and specifically did not adopt a suggested requirement that ILECs need not supply advanced network elements if the competitor could obtain those elements elsewhere. 26/

In sum, there is no legal basis for denying requesting carriers access to xDSL-equipped loops, packet switching, and interoffice transport as network elements.

#### C. xDSL Electronics are an Integral Part of the Subscriber Loop.

An "xDSL-equipped" loop, like any other loop, is a network element within the meaning of Section 251(c)(3) of the Communications Act. 27/ xDSL-equipped loops fall squarely within the statutory definition of a "network element,"

<sup>25/ &</sup>lt;u>Iowa Utilities Board v. FCC</u>, 120 F.3d at 814 (emphasis added).

<sup>26/</sup> Local Competition Order at para. 283.

<sup>27/ 47</sup> U.S.C. § 251(c)(3).

which includes all the "features, functions, and capabilities" of any ILEC "facility or equipment used in the provision of a telecommunications service." 47 U.S.C. § 153(29).

It is conceptually erroneous to define a local loop solely by reference to the physical pair of copper wires that runs from the customer's premises to the central office. The electronics necessary to transmit signals over that wire are an integral part of the loop and are included in what a carrier is entitled to purchase as a network element. 28/ Electronics may alter the transmission characteristics of a local loop (such as capacity or format), but they are part of the local loop.

Digital Loop Carrier (DLC) technology provides a case in point on why a local loop cannot be defined solely as a pair of copper wires. ILECs are turning to DLCs (also commonly called "remote terminals") because they have discovered that it is more cost-efficient to aggregate traffic at remote sites rather than build new, dedicated copper links all the way from the customers' premises to central offices ("home run copper"). Approximately 20-30 percent of customers nationwide are currently being served using DLCs, and more DLCs are being deployed by ILECs every month. 29/

<sup>&</sup>lt;u>28</u>/ The FCC has defined the local loop as "a *transmission facility* between a distribution frame, *or its equivalent*, in an incumbent LEC central office, and the network interface device at the customer premises." <u>Local Competition Order</u> at para. 380. (emphasis added).

<sup>29/</sup> See Arielle Emmet, "Multimedia: Making it Pay," America's Network, May 1, 1997 (estimating 20 percent DLC lines); "xDSL: Local Loop Access Technology," WWW3COM.COM (estimating 30 percent DLC lines). The percentage of lines served by DLCs (now between 20-30 percent nationwide) rises dramatically when

When an ILEC employs a remote DLC, there is no discrete pair of copper wires that runs all the way from the customer's premises to the central office. 30/ In most cases, ILECs transport the traffic that is concentrated at the DLCs in digital format via a high-bandwidth transmission link (generally fiber optic cable), which feeds directly into the ILEC switch. Various facilities and equipment are associated with the customer's local loop in a remote DLC environment. They include the copper wire from the customer's premises to the DLC, the line card at the DLC, the electronics at the DLC that convert analog signals to digital format, the electronics that concentrate the traffic, the electronics

one focuses on rural and suburban residential and business customers. It will also continue to increase for all customers as the demand for bandwidth rises, as the demand for second lines grows, and as the embedded copper plant becomes obsolete and uneconomical to replace with more "home-run" copper lines. ILECs increasingly are deploying DLCs (both copper T-1 and fiber-fed) to serve both existing customers (who previously were served by home-run copper) and new customers. They also are using DLCs in preparation for xDSL because shorter copper pair run lengths to the customer allow for higher speed and better quality xDSL services. See Appendices A and D for more detailed information about the use of DLCs.

<sup>30/</sup> The same is true for T-1 circuits and ISDN lines. An ISDN basic rate local loop requires ISDN line cards at either the switch or the digital loop carrier, as well as an ISDN modem at the customer premises. T-1 loops have evolved over time. Originally, T-1 capabilities could only be served on special copper cable. Later, fiber-optic electronics and medium were inserted either in the middle or terminal points of a T-1 system as that technology became available. Currently, HDSL electronics and traditional twisted copper cable are being used to provide T-1 services. As a result of this evolution, it is entirely possible (and probably quite common) that a T-1 today uses HDSL technology on twisted copper on one end of the circuit in the loop, fiber-optic electronics and medium in the interoffice transport, and traditional copper T-1 and electronics on the other end of the T-1 circuit.

that convert the electrical signals to optical ones, the fiber that carries the traffic to the central office, the electronics that convert the optical signals to electrical digital ones, and the electronics that directly integrate the electrical digital signals into the digital switching system. 31/

Customers served by DLCs thus do not have a dedicated copper link between their premises and the central office that serves them. Clearly it would be inaccurate to claim that there is no local loop associated with such customers.

Indeed, the FCC has required ILECs to provide competitors with access to these loops on an unbundled basis. 32/

Over the years, the economics associated with DLC electronics, fiber optics, and copper plant have led ILECs to increase expenditures on the fiber-fed DLC service delivery method. In fact, this method is the primary outside plant relief and network growth vehicle used by all ILECs. The increasing deployment of remote DLC technology shows how inappropriate it would be to define the loop without regard to the electronics and other technology that enables the loop to perform at the level designed for it by the ILECs. 33/

<sup>31/</sup> See Appendix C for an illustration of xDSL technology deployed in a DLC environment, and Appendix D for a more detailed discussion of the technology.

<sup>32/ &</sup>lt;u>Local Competition Order</u> at paras. 383-84.

<sup>33/</sup> Another example of the broad scope of the definition of a loop is the use of by ILECs of copper facilities to transmit concentrated digital (as opposed to conventional analog) signals to central offices. ILECs have deployed both traditional copper T-1s and the newer HDSL T-1 technologies to carry such traffic for many years.

In sum, the local loop cannot be defined by a particular type of medium or a particular set of electronics. The loop is simply a mechanism to carry traffic from a customer's premises to the central office.

# IV. COMPETITORS CANNOT COST-JUSTIFY PROVIDING THEIR OWN XDSL ELECTRONICS AND INTEROFFICE FACILITIES ON A BROAD BASIS.

## A. Competitors Will Not Have the Volumes Necessary to Justify Broad Deployment of xDSL Equipment.

To ensure the maximum development of competitive xDSL services and to ensure consumer choice and price competition for broadband services, it is essential that xDSL facilities, equipment, and functionality be available as network elements.

It is ironic that the RBOCs in their Section 706 petitions make such a passionate case for needing extra incentives to make the enormous capital expenditures and risk involved in investing in advanced technology. 34/ In doing so, they totally ignore the plight of the CLECs, who today possess tiny shares of the local market. Even if CLECs were to grow quickly, they cannot hope to have the volumes to justify the kind of local network investment that the RBOCs are contemplating.

US West's own statistics prove this out. US West argued in its Section 706 petition that because it serves many less densely populated areas, and thus has

<sup>34/</sup> We discuss in Section VII below the major xDSL rollouts by the RBOCs and GTE, which belies their claim to need extra incentives.

lower volumes of customers per switch, it needs special incentives to invest in xDSL technology to serve those customers. 35/ Clearly, if it is hard for US West to justify investing in adding xDSL for each central office serving area (when it does not even need to collocate and is not restricted in the use of switches and routers as a CLEC is), and when it has the entire local customer base over which to spread the cost of that technology, imagine how difficult it would be for each of US West's competitors to justify that investment. As US West stated in its FCC petition:

[D]eploying xDSL to a central office requires enormous capital investments: US West must install one or more DSLAMs in each central office, prepare the loops of each MegaBit Service subscriber, and cable the office to a network of ATM switching systems. 36/

#### US West also observes that

The central office equipment used to provide MegaBit service is expensive: a basic, 128-user DSLAM costs approximately \$73,000 installed (and several might be necessary), an installed ATM switching system costs approximately \$350,000, and the DS-3 networking needed to connect the central office with other central offices can cost several hundred thousand dollars. . . . 37/

<sup>35/</sup> Petition of US West Communications, Inc. for Relief from Barriers to Deployment of Advanced Telecommunications Services, FCC Docket No. 98-26, filed February 25, 1998 ("US West Petition") at 25-26.

<sup>36/</sup> US West Petition at 35.

<sup>37/</sup> Id. at 31-32. Based on conversations with vendors LCI believes the costs cited here to be low. The costs cited in footnote 40 below are more in line with current market conditions.

US West also correctly identifies residential and small business customers as the most vulnerable to being left out because of the relatively higher cost of serving them. 38/ With all this, it is genuinely puzzling why an RBOC would not conclude that the best way to recover this investment in xDSL equipment is to make it available to all carriers, thus maximizing volume.

The cost of a DSLAM, 39/ while significant, is only one of the costs facing competitors seeking to provide competitive xDSL-based services. 40/ The additional costs of collocation and installation of xDSL electronics and the cost of dedicated interoffice packet transport 41/ will inevitably skew CLEC provision of

<sup>38/</sup> *Id.* at 26.

<sup>&</sup>lt;u>39/</u> A DSLAM (Digital Subscriber Line Access Multiplexer) is the electronics attached to the central office end of a home run copper pair that enables it to have xDSL capability. <u>See</u> Appendix D at 3.

<sup>40/</sup> The cost of the DSLAM (including the necessary remote testing capability) is approximately \$100,000 for a 100-line DSLAM, with the per-line cost falling to about \$800-900 per line with higher volumes. (In its Petition at 31-32, US West has cited lower figures of approximately \$73,000 per DSLAM, but LCI's recent discussions with several vendors indicate that \$100,000 is a more realistic figure.) The ILEC is much more likely to have the volumes necessary to justify installing this equipment in every central office. A carrier the size of LCI is unlikely to have this volume of customers in every central office, at least not at the market entry point. The ILEC, in contrast, could easily reach such a volume within a short period of time. Thus, even if the cost of the DSLAM equipment appears to be comparable for the ILEC and a CLEC, the ILEC as a practical matter, would have a cost advantage in most central offices. This comparison also fails to consider the many other costs that CLECs must incur that the ILEC either need not incur, or will incur on a much lower level due to its economies of scale.

<sup>41/</sup> According to US West, the cost of the DS-3 networking needed for dedicated interoffice transport can be as much as "several hundred thousand dollars" per central office, depending on its location. US West Petition at 32.

xDSL services towards central offices serving dense commercial districts. The volume and density considerations that would drive a competitor to focus on a limited number of central offices are the same considerations that have driven the targeted nature of CLEC investment in competitive telecommunications facilities to date. Large revenue streams and high number of xDSL subscriber lines would be necessary to recoup the costs of collocation (regardless of the type), switching and transport, and other duplicative costs and expenses that would be unnecessary if xDSL-equipped loops, switching and transport could be obtained as network elements.

### B. The Initial Costs of Installing and Maintaining xDSL Facilities Will Be Prohibitive in Most Cases.

#### 1. Costs of Collocation

Most ILECs today would require a requesting carrier to physically collocate a DSLAM in each central office in order to provide competitive xDSL-based services, rather than permitting requesting carriers to obtain the loop already equipped with xDSL electronics as a network element. As a practical matter, any collocation requirement (whether physical, virtual, cageless, or otherwise) raises competitors' costs well beyond the level that the ILEC will incur, on a per-customer basis, to provide the same service. Collocation requirements of any kind thus could have the practical effect of eliminating an entire class of customers -- those for whom duplicate CLEC investment cannot be justified -- from enjoying the benefits of competitive and innovative choices in broadband telecommunications services.

#### 2. Physical Collocation Costs

Central office space availability is a problem in many locations today, and may become a more widespread problem in the future as local competition takes hold. Where space is unavailable, requiring physical collocation means that customers served by such end offices will not enjoy the benefits of competitive broadband services. At least one CLEC has reported that in as many as 15% to 20% of central offices where it desired to physically collocate for the purpose of providing xDSL services, ILECs have claimed that no space was available. 42/ This was apparently the case even in central offices that primarily served residential customers.

Even where central office space is not a problem, requiring collocation and installation of DSLAM equipment is anticompetitive because it raises rivals' costs without any countervailing efficiency benefits. Collocation requirements also have the practical effect of forcing competitors to target only the most dense central offices, because competitors must be able to spread the added costs of collocation (which the ILECs do not incur) over a sufficiently large number of customers to make it profitable to compete against the ILEC's xDSL offerings. By forcing competitors to install their own DSLAM equipment (and thus to incur the costs of

<sup>42/</sup> See Comments of Covad on RBOC Section 706 petitions, FCC Docket Nos. 98-11, 98-26, 98-32, filed April 6, 1998, at 14. See also Comments of AT&T on Bell Atlantic Section 706 Petition, filed April 6, 1998, at 18 n.34.

collocation), ILECs can drive competitors' costs up to the point where it is not possible to compete for customers in many central offices (if at all).

For illustrative purposes, consider the consequences of a collocation requirement in one of the Texas LATAs (Dallas/Fort Worth). SBC in Texas has required competitors to install a minimum of a 100 square foot collocation cage. 43/
This requirement is, of course, patently absurd in light of the fact that the equipment is no bigger than a desktop computer without a monitor, but it is typical of many ILECs. Assuming an average cost for such physical collocation of about \$100,000 in non-recurring charges 44/ and approximately \$1500 in monthly recurring charges, and amortizing the non-recurring charges over ten years (a reasonable period of time over which a competitor could expect to recoup its non-recurring costs), the cost of such collocation would be roughly \$2300 per month.

Even if all other network elements are priced at TELRIC rates, a CLEC therefore will face a severe cost disadvantage vis-a-vis the ILEC in the provision of xDSL

<sup>43/</sup> See Southwestern Bell Telephone Company, Physical Collocation Tariff, Section 7 (as revised on 3/9/98).

<sup>44/</sup> This figure is a fairly typical ILEC non-recurring charge for a 100 square foot collocation space. See, e.g., Comments of Covad Communications Company on RBOC Section 706 petitions, filed April 6, 1998, at 15 ("Comments of Covad on RBOC Petitions"). Southwestern Bell has recently amended its collocation tariffs to reflect lower rates prescribed by the Texas PUC in arbitration proceedings, so it is not clear whether the average collocation charges would fall within the assumed range. But, as we discuss below, even if the assumed \$100,000 collocation charge were significantly reduced (by a factor of ten) to \$10,000, and the cage size were brought down from 100 to 7.5 square feet, the fact remains that many central offices would be unprofitable to serve via collocation.

services that is directly attributable to the collocation requirement. (As we discuss further below, this calculation does not include all the other costs that will be higher for a CLEC than they would be for the ILEC -- e.g., duplication of the interoffice network).

Assuming 80 per cent 45/ of all local loops in the Dallas-Fort Worth LATA are capable of supporting xDSL services and assuming a penetration rate of 0.5 percent (equivalent to one third of LCI's 1.5 percent nationwide long distance market share), a CLEC that wants to provide xDSL services will face a cost disadvantage attributable solely to its need to collocate ranging from \$5.50 per line (per month) in the central office with the greatest concentration of lines to \$1444 per line (per month) in the central office with the fewest lines. 46/ Put differently, depending on the central office, it would cost the CLEC between \$5.50 per line and \$1444 per line more than it would cost the ILEC to provide xDSL services due solely to the collocation requirement.

Using this example, and assuming that a CLEC somehow could profitably serve customers in central offices in which its costs were \$10 per month per line more than the ILEC's (which is unlikely to be possible, given that the price

<sup>45/</sup> This assumption is actually on the high side. In reality, fewer than 80 percent of the loops are likely to be capable of supporting xDSL services, and therefore the number of potential customers in each central office will be even lower.

<sup>46/</sup> The source for the number of lines per central office is the 1995 ARMIS data on switched access lines.

of current xDSL offerings range anywhere from \$40 to \$150 per line per month), a CLEC could profitably offer xDSL services only in five of the 112 central offices in the Dallas-Fort Worth LATA. This leaves customers in 107 central offices who would not be offered competing xDSL services by CLECs. If one were to assume that a CLEC could only absorb a \$5 per line (per month) cost differential vis-vis the ILEC (a more reasonable, though still probably unrealistic, assumption) a CLEC could not profitably offer the service in *any* of the 112 central offices. That is so because, based on our calculations, there is no central office where the cost differential between the CLEC and the ILEC is as low as \$5.00. 47/

Even if the non-recurring cost of physical collocation were reduced by many factors to a more reasonable level (such as the \$10,000 for cageless collocation proposed by Covad) 48/ and the minimum space requirement were only 7.5 square feet (for example, as agreed to by BellSouth in the Tennessee Section 271 proceedings), 49/ 48 central offices in the Dallas-Fort Worth area (almost half of the

<sup>47/</sup> The point here is that because the CLEC must incur substantial up-front costs in connection with collocation, it must spread those costs among its customers in each central office. The CLEC will always have a cost disadvantage vis-a-vis the ILEC because of its need to incur collocation costs. Even if one assumes that the CLEC can absorb some of this cost differential (through lower overhead or customer acquisition costs, for example), it still will not be able to cost-justify serving customers in less dense central offices.

<sup>48/</sup> Comments of Covad on RBOC Petitions at 15.

<sup>49/</sup> Here we prorate the assumed \$1500 monthly recurring charge, based on the smaller cage size (\$15 per square foot).

total) would not qualify as profitable, assuming that the CLEC could absorb a cost differential vis-a-vis the ILEC of \$5 per line per month.

Of course, any cost differential is discriminatory and anticompetitive. CLECs could absorb such a differential only if their other expenses (e.g. marketing overhead) could be reduced below the level incurred by the ILEC. More important, however, the figures just discussed do not include the CLECs' likely much higher transport and switching expenses and higher per line installation, maintenance and testing, engineering, and other costs. These additional higher per-customer costs are discussed below. Thus, under even the highly optimistic (and unrealistic) scenario presented above, many central offices would be unprofitable to serve if the entrant were forced to install its own xDSL facilities.

### 3. Virtual, "Cageless," and Other Types of Collocation

Some ILECs have made available or have proposed virtual collocation options or variations on physical collocation (such as "cageless collocation"), which are designed to deal with the high costs of physical collocation and the space limitations in central offices that could prevent physical collocation. 50/

Such alternatives are no solution. They entail economic obstacles in the form of real and hidden costs when implemented in the real world. For instance, virtual collocation requires the CLEC to gain ILEC approval for the type

<sup>50/</sup> See, e.g., Pre-Filing Statement of Bell Atlantic-New York, Petition of New York Telephone Company for Approval of its Statement of Generally Available Terms and Conditions Pursuant to Section 252 and Draft Filing of Petition for InterLATA Entry, NY PSC Case No. 97-C-0271, filed April 6, 1998, at 16.

and size of the equipment placed. In addition, ILECs charge prices they set unilaterally for the maintenance of equipment. ILECs also typically mandate that the equipment be fully provisioned, thereby excluding the prudent business practice of deploying assets incrementally.

Virtual collocation also, by definition, adds unnecessary costs that would not need to be incurred if a CLEC could obtain xDSL-equipped loops as network elements. Virtual collocation and other methods also are either subject to dispute or are not yet developed or tested. ILECs generally have been reluctant to explore alternatives to physical collocation until forced to do so by regulators. The CLEC and ILEC industries have spent the last two years engaged in seemingly endless legal fights over the details of these issues in interconnection arbitration proceedings that continue to this date on a state-by-state basis.

Finally, with virtual, cageless, or physical collocation, a CLEC still cannot serve on a parity basis the significant and growing number of customers who are served by the ILECs using DLCs (approximately 20-30 percent of all subscriber lines nationwide, and growing). The issues surrounding competitor access to DLC loops (whether or not equipped with xDSL capability) have yet to be resolved. 51/

<sup>51/</sup> ILEC interconnection agreements continue to put the CLEC at a competitive disadvantage when it comes to obtaining loops equipped with DLC electronics. ILECs generally provide unbundled local loops served on DLCs only after passing special construction costs and time delays onto the CLEC. These charges are either for construction of new "home run" copper plant placed by the ILEC or for reverse DLC equipment (required to de-multiplex back to the copper analog signal level) located in the Central office. All these details add unnecessary costs and delay for the CLEC.

#### 4. Interoffice Switching and Transport Costs

Regardless of the type of collocation required for the DSLAM, access to transport from the central office to a CLEC's data switching systems is still necessary. CLECs must have the option of employing the ILEC's interoffice transport and switching to carry the xDSL traffic of their customers to their own networks, just as they do for carrying conventional local exchange traffic. Without such an option, a CLEC would be forced to build duplicate interoffice transport and switching facilities from every central office that would be cost-prohibitive, at least until the CLEC has a large, established base of customers served by broadband facilities at each central office. 52/

The cost of duplicating the ILECs' interoffice network -- to bring broadband traffic from each central office to the CLEC's packet switch -- would be prohibitive. 53/ As the FCC recognized in ordering ILECs to provide network element access to the ILEC interoffice transport network ("shared transport"), the volume efficiencies of the ILEC network are enormous. Lack of access by competitors to that shared interoffice network would pose a significant barrier to entry, as the FCC found. 54/ Similarly, if competitors had to duplicate the ILEC

<sup>52/</sup> CLECs that target only a handful of central offices for xDSL service might find it economic to provide their own dedicated interoffice transport, but to serve all central offices (and thus all potential customers), the cost of such transport would be prohibitive.

<sup>53/</sup> See US West Petition at 23 and 31-32 (regarding costs for backhauling data traffic).

<sup>54/</sup> See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, 95-185, Third Order on

interoffice packet network in order to provide competing broadband telecommunications services to all central offices, the costs would be prohibitive. <u>55</u>/

Because of the broadband capabilities of xDSL loops, dedicated interoffice transport to carry such traffic has become increasingly expensive (for example, \$2,000 per month for a DS-3 circuit of 5 miles in the BellSouth region). 56/ As a result, a CLEC is unlikely to offer xDSL services to customers served by central offices with few potential subscribers (e.g., central offices serving small business and residential customers and central offices in less densely populated areas). 57/ Only the ILEC, which already has an interoffice network, could justify serving all those locations.

Reconsideration, FCC 97-295, released August 18, 1997, 12 FCC Rcd 12460, petitions for review pending, Southwestern Bell Tel. Co. v. FCC, Nos. 97-3389 et al. (8th Cir.), at paras. 25-37. The FCC recognized that if competitors had to duplicate the ILEC interoffice network (even through use of unbundled dedicated interoffice transport), the costs of such duplication would be enormous: "[T]he failure of the incumbent LEC to provide access to all of its interoffice transport facilities on a shared basis would significantly increase the requesting carriers' costs of providing local exchange service and thus reduce competitive entry in the local exchange market." Id. at para. 34.

- 55/ Requesting carriers also would require access to the ILEC's packet switches, just as they require network element access to the ILEC circuit switches. Switching, router, and interoffice transport, whether circuit-switched or packet-switched, clearly fall within the definition of network elements under the Act. 47 U.S.C. § 153(29). DSLAMs also are now being made with packet switching capability built in.
- 56/ The bandwidth required for interoffice transport for xDSL services would start at the DS-3 or OC-N level.
- <u>57/</u> In those circumstances in which placing a DSLAM in a central office can be cost-justified, prohibitions on placing equipment with switching functionality in collocation cages prevent efficient network design and optimization.

#### 5. Maintenance, Engineering, Technical, and Other Costs

Finally, regardless of the form of collocation used, collocation will also impose additional costs on the CLECs over and above equipment and collocation costs. These include, for example, the cost of equipment installation and maintenance, installation of service, coordination with ILECs and CLECs for the placement of the equipment and delivery of service, and engineering for the location and installation of equipment. Because CLECs do not have maintenance personnel physically located in the ILEC central office, remote maintenance testing and diagnostic equipment is critical, and will create additional upfront and ongoing costs for CLECs that ILECs do not incur. Legal fees to negotiate and arbitrate interconnection agreements, and resolve disputes with ILECs about collocation, interconnection, and service quality (to name a few) are also significant deterrents to rollout of competitive xDSL services, and create significant delay and time-to-market disadvantages for competitors.

The far lower customer volumes that CLECs will have, relative to the ILEC (which today starts with almost 100 percent of the local customer base), also mean that the CLEC's per-customer costs will be far higher. For example, the costs of hiring and dispatching technicians to disconnect and reconnect lines on the DSLAM and to maintain the equipment would be prohibitive in the absence of substantial volumes of customers in each central office. Although many of these costs will also be borne by ILECs, the ILECs will have the volumes necessary to bring the per-customer costs down to a reasonable level. The ILECs also will have

the volumes necessary to justify a mass-market approach to broadband telecommunications services, rather than targeting certain central offices, which the CLECs of necessity must do.

In sum, the economics simply do not justify competitive provision on a broad geographic basis of xDSL services, in the absence of availability of xDSL-equipped loops, packet switching, and interoffice transport as network elements.

## V. ACCESS TO XDSL CAPABILITY BY ILEC COMPETITORS WILL HELP ENSURE A COMPETITIVE ENVIRONMENT FOR ISPS

Providing CLECs with access to xDSL capabilities in the ILEC network also should help to ensure a competitive environment for Internet Service Providers ("ISPs") who require access to customers, as pointed out, for example, by the Commercial Internet Exchange Association in comments filed in opposition to the RBOC petitions. 58/ If an ILEC is the only provider of xDSL services, it could potentially partner with an ISP, perhaps its own affiliate ISP, on an exclusive basis. Some of the RBOC xDSL plans already include the bundled provision of a high-capacity line with Internet access service. 59/ Exclusivity would guarantee that

<sup>&</sup>lt;u>58</u>/ <u>See</u> Comments of Commercial Internet Exchange Association, filed April 6, 1998, on Bell Atlantic Petition, CC Docket No. 98-11, at 2.

<sup>&</sup>lt;u>59/</u> For example, Bell Atlantic plans to combine the monthly charge for the high-speed line with Internet access service for a single price. "Bell Atlantic to Offer High-Speed Links to Net," <u>Washington Post</u>, June 4, 1998, at E3.

customers subscribing to xDSL services from the ILEC would have high-speed access to the services of only one ISP. 60/

Permitting CLECs to obtain network element access to xDSL technology would better serve the objective of providing end user choice among ISPs. CLECs today are already partnering with ISPs to provide them an alternative to the ILEC's network. If CLECs have access to xDSL network elements, they can provide end users with high-speed access to the ISP of their choice. Most CLECs have an incentive not to enter into exclusive arrangements with ISPs for the simple reason that the market share of the ISP will determine the CLEC's share of xDSL services. Such exclusivity is not likely to be profitmaximizing. CLECs, therefore, have an incentive to partner with as many ISPs as possible. ILECs will also have the same incentive not to enter into exclusive or discriminatory arrangements if they face competition; if they are able to maintain an effective monopoly, however, the opposite will be true.

In sum, CLEC access to xDSL loops not only furthers competition in the provision of broadband telecommunications services, but also guarantees customers greater choice among ISPs.

<sup>60/</sup> This scenario is not unlike the case of cellular carriers, who now are allowed to partner with a single long-distance carrier on an exclusive basis. Subscribers of these wireless carriers are not allowed to subscribe to the services of competing long-distance carriers on a 1+ basis.

# VI. FENCING OFF ACCESS TO ILEC DATA NETWORKS WILL LIKELY CREATE A DOMINANT LEC IN BOTH DATA AND VOICE IN THE FUTURE.

The notion of creating a much more liberal regulatory regime for packet-switched networks and data services, while retaining the system envisioned by the 1996 Act for circuit-switched networks and voice services, is not legally or technically sustainable. 61/ The Communications Act does not distinguish between the transmission of voice or data or between circuit switched and packet switched telecommunications. To foster the evolution of technology and service, regulators should refrain from drawing lines on the basis of technology and cost assumptions that will necessarily become obsolete as technologies develop and cost characteristics change.

It is widely acknowledged that in many cases, the same facilities are used for both packet-switched and circuit-switched networks, and that voice and data services are rapidly converging. As Intermedia noted in its comments to the FCC on the RBOC petitions:

[T]here is no bright line between packet switched and circuit switched networks and services. In fact, "plain old telephone service" is routinely provided over packet switched data networks as well as circuit switched networks. Moreover, a single telephone call can originate on the circuit switched network, be transported over a packet switched data network, and terminate back on a circuit switched network. 62/

<sup>61/</sup> The FCC has recognized that the term "network element" must "accommodate changes in technology." <u>Local Competition Order</u> at para. 259.

<sup>62/</sup> Comments of Intermedia, Summary at 1.

Data has long traveled over circuit-switched networks designed primarily for voice telephony. Increasingly, purveyors of "Internet telephony" are learning how to make voice calls traverse packet-switched networks. With the help of electronics, customers are increasingly using the public Internet and other packet-data networks to carry voice traffic.

The merger of separate voice and data networks into combined broadband telecommunications networks (and the growth in the share of data traffic relative to voice traffic) mean that virtually all voice traffic may soon be carried by the same broadband telecommunications networks that carry data. xDSL technology already combines voice and data on the same line from the customer's premises to the central offices. Several companies have stated that they are carrying or will carry voice as well as data over their packet networks. Sprint recently announced, for example, plans to carry all its voice and data traffic over the same ATM (asynchronous transfer mode) based broadband network. 63/

These evolutionary trends all point to the same inevitable result: voice and data networks are merging, and where data goes, voice will follow. 64/ This is so because voice is narrowband and can readily be accommodated on broadband networks, and packet switching can be more efficient than traditional circuit

<sup>63/</sup> See "Sprint Unveils Revolutionary Network," Press Release, June 2, 1998, at www.sprint.com/sprint/press/releases; Communications Daily, June 3, 1998, at 2-3.

<sup>64/</sup> This is apparent when on examines the rate at which data traffic is growing relative to voice. See Section II, above.

switching. 65/ Thus, any regulatory distinction drawn between voice and data or between packet and circuit switched networks is artificial and likely to be unsustainable. Any policy that effectively limits competitors' access to ILEC advanced network capabilities will ensure that ILECs will remain dominant providers of voice services, as well as ensuring their dominance in providing broadband telecommunications services.

## VII. ILECS ALREADY HAVE STRONG INCENTIVES TO INVEST IN XDSL TECHNOLOGY.

Strong incentives already exist for the RBOCs to deploy xDSL technology broadly. The ability of xDSL electronics to leverage much of the embedded telecommunications infrastructure makes it a cost-effective method for the delivery of broadband telecommunications services to small-businesses and consumers. 66/ This ability to use assets that are already in the ILEC's network,

<sup>65/</sup> Another less obvious trend is the evolution of network architecture from hierarchical to a flatter, more distributed topology. Packet switching technology is making this evolution possible since each individual packet contains headers that identify both the source and destination of the packet. The packet of information is not confined to a particular information path. The distribution of information, whether voice or data, will no longer be restricted to hierarchical paths. The development of broadband networks capable of carrying both voice and data, whose nodes are distributed in a non-hierarchical form, is a significant development in network architecture.

<sup>66/</sup> See generally Appendix D. xDSL technology exploits existing copper plant, fiber feeder systems, and loop electronics in both existing and newer-vintage DLCs. ILECs have employed HDSL technology for several years, which means that the cable-and-pair assignment, provisioning, and troubleshooting processes, as well as support systems, which are needed to enable the widespread xDSL use, are already in place or can be easily enhanced to handle additional xDSL loops.

coupled with strong demand for higher-bandwidth services, is the reason that xDSL electronics are already being deployed by incumbent LECs, and, to the extent they are able to do so given ILECs resistance, by CLECs.

The RBOCs' own actions belie their claim that they lack incentives to deploy xDSL technology in their networks. The group of U.S. companies collectively known as the Joint Procurement Consortium (which includes all of the regional Bell operating companies -- RBOCs -- except Bell Atlantic) has plans to deploy more than 2 million ADSL lines over the next five years. The Yankee Group predicts than such deployment will occur before the year 2001.

As one example, US West announced recently that it has prepared 226 central offices in its 14-state region (covering 5.5 million access lines) to provide ADSL offerings by June 1998. It already has an ADSL offering in Phoenix, Arizona. For residential customers, US West plans to offer ADSL services for merely \$40 per month plus installation fees. For businesses, it intends to offer slightly higher speed service for \$65 per month plus installation fees. 67/

BellSouth and SBC recently announced major ADSL rollouts in their regions. BellSouth is planning to make ADSL service available to over 1.7 million lines in seven markets this year with expansion to 23 additional markets in 1999. 68/ SBC announced that its Pacific Bell operating company would begin

<sup>67/ &</sup>quot;Bells, GTE, and Computer Giants Say ADSL Working Group Will Speed Deployment," Telecommunications Reports, February 2, 1998, at 23-24.

<sup>68/ &</sup>quot;BellSouth Plots Ambitious ADSL Plan," Multichannel News, May 25, 1998, at 1; News Release, "BellSouth Announces Aggressive 30 Market Roll-Out of Ultra-

offering ADSL Internet access service to all or parts of 200 communities in California by September of this year, and expects its service to reach 4.4 million homes and 650,000 business customers. 69/ GTE has also unveiled plans to offer ADSL in approximately 300 central offices in parts of 16 states beginning in June 1998 for both residential and business customers. Its target monthly rates are between \$30 and \$250, depending on the type of service. 70/ Bell Atlantic recently announced its plans for rolling out ADSL services, beginning in September, with expectations of reaching 2 million lines by the end of 1998 and 5 million more by the end of 1999. 71/ Ameritech is also rolling out ADSL in its home region. 72/

The facts show that the RBOCs are actively deploying xDSL technology under the current regime, without any special incentives or bribes.

There is no reason to assume that the RBOCs will not continue the deployment of xDSL in their networks. They do not need relief from regulatory requirements to

High Speed BellSouth.Net FastAccess ADSL Internet Services," May 20, 1998, at www.bellsouthcorp.com.

<sup>69/ &</sup>quot;SBC's Pacific Bell Unit Unveils ADSL Plans, Files Pricing Tariff," Telecommunications Reports, June 1, 1998, at 34.

<sup>70/</sup> See "GTE Jumps Into xDSL Game as UAWG Works on Standard," Telecommunications Reports, April 20, 1998, at 18; "GTE to Offer Ultra-Fast Internet Access," April 13, 1998 Announcement on GTE website, www.gte.com/g/news/adsl041398.html.

<sup>71/ &</sup>quot;Bell Atlantic to Offer High-Speed Links to Net," Washington Post, June 4, 1998, at E3.

<sup>&</sup>lt;u>72/</u> <u>See</u> BellSouth Plots Ambitious ADSL Plan," <u>Multichannel News</u>, May 25, 1998, at 54.

create incentives for such investments. Such incentives already exist, and are powerful. The ILECs' request for deregulated treatment of their advanced technology and services is, in effect, a request for permission to charge supracompetitive prices for their xDSL services -- something they would be able to do only if shielded from competition.

#### CONCLUSION

The denial of CLEC access to elements of broadband networks will almost certainly mean that ILECs who have monopoly control over narrowband (voice) networks today will become monopoly providers of broadband (including voice) services tomorrow. Enforcing the Act's market-opening provisions equally for all technologies and services is the best way to ensure wide deployment of advanced technology and the broad availability of competitive choices in advanced telecommunications services for all consumers.

### APPENDIX A

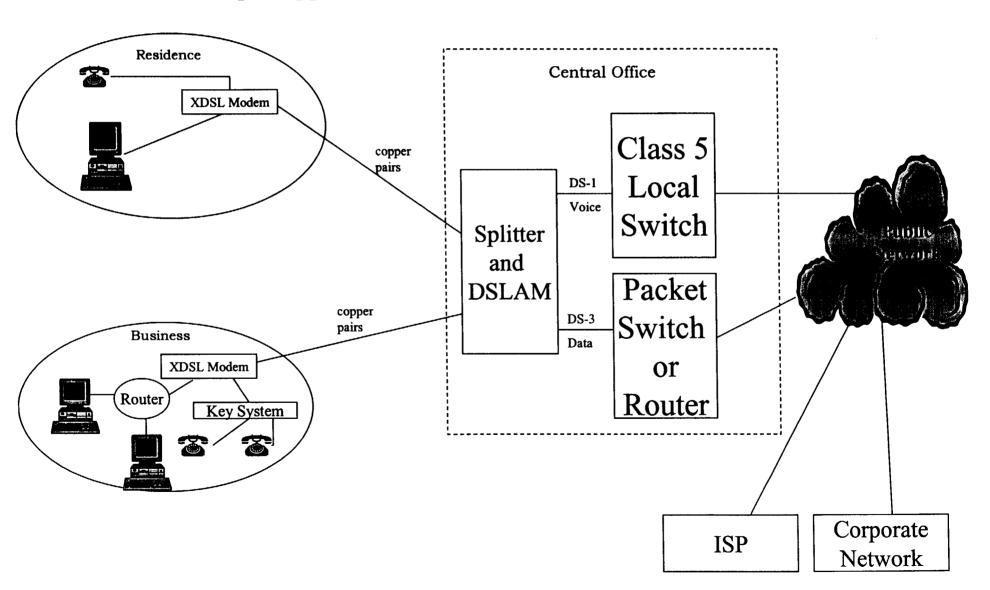
### DSL Technologies

Technology	Speed(s)	Distance Limitations	<u>Characteristics</u>
ADSL	1.544 Mbps to 8.448 Mbps (Downstream) and 16 kbps to 640 kbps (Upstream)	9,000 to 18,000 feet	Asymmetric (Different Transmit and Receive Speeds) One Wire Pair
R-ADSL	1.544 Mbps to 8.448 Mbps (Downstream) and 16 kbps to 640 kbps (Upstream)	9,000 to 18,000 feet	Rate Adaptive Asymmetric One Wire Pair
HDSL	1.544 Mbps	15,000 feet	Symmetric (Same Transmit and Receive Speeds) Two Wire Pairs
SDSL	1.544 Mbps	10,000 feet	Symmetric One Wire Pair
VDSL	12.96 Mbps to 51.84 Mbps (Downstream) and 1.5 to 2.3 Mbps (Upstream)	1,000 to 4,500 feet	Asymmetric One Wire Pair

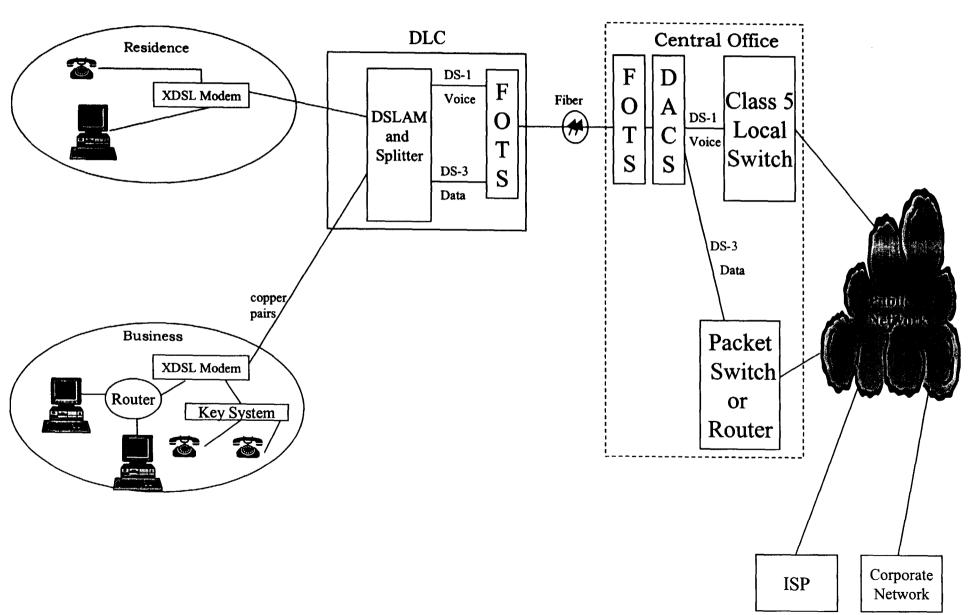
Source: xDSL: Local Loop Access Technology, WWW.3COM.COM.

Appendix B

xDSL Loop: Copper Between Customer Premises and Central Office



Appendix C xDSL Loop: Copper Between Customer Premise and DLC



#### APPENDIX D

#### BACKGROUND ON XDSL TECHNOLOGY

#### **Limitations of Conventional Copper Loops**

The low bandwidth of local loops today has little to do with the actual copper line itself. It results from filters around the core of public switched telephone networks that limit voice bandwidth to 4 khz to ensure high-quality voice transmission. 1/ Voice-grade modems transmit analog data signals through the network without alteration, but only signals within the 4 khz range. The network treats such data signals exactly as it does voice signals. Without filters around the core of voice networks, copper access lines could pass higher-frequency signals but with substantial attenuation of the signal. The need to maintain voice quality on public switched telephone networks, therefore, limits the frequency (and thereby bandwidth) that could be exploited by copper access lines.

#### The Potential of xDSL Technology

xDSL technology allows the transmission of signals over copper access lines at frequencies in the megahertz range. The higher frequencies, however, increase signal attenuation and introduce distance limitations on robust transmission of data. Greater signal degradation over greater distances also contributes independently to the distance limitations. A digital subscriber line ("xDSL") is basically a copper access line with a pair of modem-like devices at either end of the line. 2/Splitterless xDSL (such as, e.g., "ADSL-lite") modems today combine coding and splitter (that isolates 4 khz for voice) functionalities in a single device that can be plugged into a telephone jack. With xDSL electronics at either end of copper local loops, both voice and data can be transmitted on the same physical wire, eliminating the need for separate wires for voice and data. Because it allows both voice and data to be carried on the same wire, thus leveraging an existing network element, xDSL is considered an enabling technology rather than a replacement technology.

<sup>&</sup>lt;u>1</u> See General Introduction to Copper Access Technologies, at www.netspeed.com/tutorial.html.

<sup>&</sup>lt;u>2</u> <u>Id</u>.

xDSL technology is often referred to as xDSL, where the "x" stands for the many variations on the theme of using modems/splitters to carry voice and data over the same physical copper line. Appendix A summarizes the salient characteristics of the various xDSL technologies. Among xDSL technologies, ADSL has received the most attention.

#### Limitations on Full Deployment of xDSL

Not all copper local loops with copper can be enabled with xDSL electronics. Depending on the type of xDSL technology, there are distance limitations that preclude some loops from being xDSL-enabled. 3/ A customer must be within the relevant distance from the ILEC's central office (if the copper portion of the loops runs all the way to the central office), or from the DLC that serves the customer, in order to receive xDSL services.

The distance limitations mentioned above are due to signal attenuation that arises from the use of frequencies in the megahertz range. Greater signal degradation over greater distances also contributes independently to the limitations. The higher the desired bandwidth and the greater the quality of signal transmission, the less distance there can be between a customer's premises and termination point of the copper segment.

Additionally, some xDSL technologies, such as ADSL, are asymmetric, meaning that the attainable downstream speeds are higher (1.5 Mbps for ADSL) than upstream speeds (384 kbps for ADSL). Symmetric xDSL formats carry information at the same speeds in both directions. Applications of asymmetric xDSL technologies are more consumer (residential) oriented, while applications of symmetric xDSL formats better suit the needs of businesses.

#### Two Variations of xDSL-equipped Loops

Since the copper portion of a local loop may run from a customer's premises to either a central office or a digital loop carrier ("DLC"), there are two main variants of xDSL loops.

Home Run Copper Loops. The first type of xDSL loop can be referred to as a "home-run copper xDSL loop." This means that the copper portion of the loop extends from the customer's premises all the way back to the central office. Currently, approximately seventy percent (70%) to eighty percent (80%) of

<sup>3</sup> The various types of DSL technologies and their distance limitations are summarized in Appendix A.

subscribers in the United States are served by local loops with copper extending all the way from the customer's premises to the central office. 4/

Even if within the required distance, the local loop must neither pass through load coils, have extensive bridge taps (extensions or spurs of a particular copper pair to other homes or routes in the feeder plant) nor be of poor copper quality. Additionally, copper loops that are adjacent in the same binder group can have loop assignment restrictions with high-speed xDSL technology because the associated high frequency produces interference. Nevertheless, since there are roughly 150 million total copper local loops in the U.S., the number of copper lines that qualify for xDSL using "home run" copper as the service delivery method is a significant percentage. 5/ Given the aggressive deployment of DLC technology nationwide, home run copper will continue to decrease as a percentage of the total.

Enabling "home-run" copper lines with xDSL technology capable of delivering both voice and data requires a key piece of electronics at the central office: a Digital Subscriber Line Access Multiplexer ("DSLAM") with modulating and data multiplexing functionalities that communicates with the xDSL modem at the customer's premises. An xDSL loop that passes through a splitter before it connects to a DSLAM in the central office generates separate voice (at the 4 khz range and in analog format) and data (in a digital, packetized format such as Asynchronous Transfer Mode ("ATM")) streams that can be sent to voice and data switches respectively. A "home-run" copper xDSL loop, therefore, transmits voice and data as a single stream from the customer premises to the central office where it emerges as two discrete streams on the output side of a splitter and DSLAM. (see Attachment B). Recent advances in technology by equipment manufacturers allows for the splitter and DSLAM functionality to be combined into one piece of equipment. This development allows for the separate voice stream to be in a digitized format (e.g.- TDM) at a higher level (e.g.- DS-1 bit rate) which, together with the high speed data stream (e.g.- DS-3 bit rate & ATM format), are both converted to a switch-ready format.

Remote Digital Loop Carrier (DLC) Loops. DLC electronics have been deployed by ILECs for at least 20 years. Basically this equipment is a remote

<sup>4/</sup> See Arielle Emmet, "Multimedia: Making it Pay," America's Network, May 1, 1997 (estimating 20 percent DLC lines); "xDSL: Local Loop Access Technology," WWW3COM.COM (estimating 30 percent DLC lines).

<sup>5 &</sup>lt;u>See</u> Statement of Charles J. McMinn, President and CEO, Covad Communications Company, before the Subcommittee on Communications, Committee on Commerce, Science, and Transportation, United States Senate, April 22, 1998, Transcript at 18.

extension of the switch that performs the analog to digital conversion of copper pairs as well as concentration and multiplexing functions in order to backhaul dialtone services over fiber or T1 copper systems to the ILEC central office. This technology has been the primary relief vehicle for the local loop outside plant over the last 10 years, in lieu of large copper cable growth and replacement expenditures. Additionally, in the last ten years the digital voice streams originating from the remote DLCs have been integrated directly into the ILECs voice switch without demultiplexing to the baseband analog level and format.

If the copper portion of a local loop extends from the customer's premise only to the remote DLC that serves the customer, enabling the loop to exploit xDSL technology requires the placement of equipment with DSLAM and splitter functions at the remote site. (see Attachment C). The voice and data streams are separated and multiplexed at the DLC and carried to the central office in Time Division Multiplexing ("TDM") and Asynchronous Transfer Mode (ATM) (packetized) formats, respectively. In a fiber-fed DLC scenario, the two electrical streams are converted to optical streams at the remote location and are then carried over the same fiber to the central office. At the central office, the two telecommunications streams are converted back to separate electrical streams via a Fiber Optic Terminal System ("FOTS") and a Digital Cross Connect System ("DACS") and are ready to be switched by a circuit switch for voice and a packet switch for data. If existing or new copper-based T-1s are used instead of fiber for transport from the DLC to the central office, the conversion to and from optical signals can be omitted.

Same voice and data streams. The same voice and data streams emerge at the central office whether or not home run copper or DLC technology is used. The partial copper xDSL loop entails electronics between the customer's premises and the central office, but as with the home-run copper xDSL loop, two switch-ready voice and data streams emerge at the central office. Thus, the inputs and outputs are the same in both scenarios despite the different set of electronics in between.

The key is for the CLEC to get parity at the digital signal level (e.g., DS-1, DS-3, OC-N, etc.) and in signal format (e.g. ATM, TDM, etc.), and have cross-connection or a hand-off point for a switch ready (e.g. voice, data) signal. The relevant analogy to this situation is the fact that ILECs offer unbundled local loop T-1s in the same digital format and at the same digital level, regardless of whether the T-1 is delivered by home-run copper to the central office or partial copper to the DLC and fiber back to the central office.

Irrespective of the particular transmission method employed -- whether home-run copper or copper to the DLC plus fiber to the central office -- it is technically feasible with current vendor technology to hand off and pick up the voice and data streams carried over an xDSL loop at the central office on a per customer or carrier basis.

# Before the FEDERAL COMMUNICATIONS COMMISSION Washington, DC 20554

RECEIVED

In the Matter of:

Petition for Expedited Declaratory Rulings

OCT 15 1998

FEDERAL COMMUNICATIONS COMMISSION

OFFICE OF THE SECRETARY

## PETITION OF LCI INTERNATIONAL TELECOM CORP. FOR EXPEDITED DECLARATORY RULINGS

A "Fast Track" Plan To Expedite Residential Local Competition And Section 271 Entry Through Establishment Of Independent RBOC Wholesale And Retail Service Companies

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January 22, 1998

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#### INTRODUCTION AND EXECUTIVE SUMMARY

This petition (along with companion petitions to be filed in New York and Illinois) is aimed at breaking the current stalemate that is denying consumers -- and especially residential consumers -- the benefits of the Telecommunications Act of 1996 (the Act). Congress intended to open "all telecommunications markets to competition." 1/ Nearly two years after the Act's

Joint Statement of Managers, S. Conf. Rep. No. 104-230, 104<sup>th</sup> Cong., 2d Sess. 1 (1996) ("Conference Report"). As this Commission has stated, "[t]he fundamental objective of the 1996 Act is to bring to consumers of telecommunications services in all markets the full benefits of vigorous competition" through "[t]he opening of all telecommunications markets to all providers [which] will ... bring new packages of services, lower prices, and increased innovation to American consumers." Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act, as amended, First Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-149, 11 FCC Rcd 21905, 21911, para. 7 (1996) ("Non-Accounting Safeguards Order"), Order on Reconsideration, FCC 97-52 (rel. Feb. 19, 1997); Second Order on Reconsideration, 12 FCC Rcd 8653 (1997), petition for review denied sub. nom., Bell Atlantic v. FCC, No. 97-1432 (D.C. Cir. decided Dec. 23, 1997); petition for review pending sub. nom. SBC Communications v. FCC, No. 97-1118 (D.C. Cir. filed March 6, 1997) (held in abeyance pursuant to court order filed May 7, 1997).

passage, however, one conclusion is inescapable: its promise of local competition has not been realized. And as a result, RBOCs have not earned the right to provide interLATA service either. 2/

The absence of residential competition in the local market is a particular disappointment, especially for a company such as LCI International Telecom Corp. (LCI) that has made the residential market an important focus of its business. A significant portion of LCI's gross revenue is derived from service to residential subscribers, and they are a critical focus of LCI's business. LCI competes for those subscribers by providing superior service at competitive prices over advanced network facilities, primarily its own. For example, LCI has benefited consumers by pioneering innovative flat rate pricing plans (now widely copied in the industry). We recently became the first carrier to offer residential customers exact billing rounded to the nearest second, not the next minute.

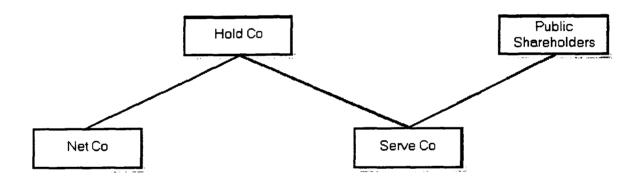
LCI is committed to compete in the local market, including extending new local service choices to its millions of residential subscribers. To do so, we inevitably must make use of the ubiquitous network facilities of the ILECs, the only facilities that reach out to every subscriber in the nation.

Unfortunately, however, to date we have met only frustrating obstacles, especially in the three key areas of: (i) operations support systems (OSS); (ii) availability of unbundled network element (UNEs); and (iii) pricing. LCI has concluded that these problems are not transitional because they stem from an inherent conflict of interest between an RBOC's dual role as both network supplier and service provider. Any incentive the RBOC might have to sell the use of its

Illustratively: (i) this Commission, the states and the courts are embroiled in thousands of disputes over highly complex technical, operational and pricing issues; (ii) residential consumers have no material local exchange service choice as demonstrated by the fact that RBOCs still serve virtually 100% of the residential market in their regions; (iii) local service choices for business customers is almost as sparse; (iv) RBOCs are not vigorously entering each other's local exchange markets; and (v) no RBOC to date has been able to meet the OSS requirements that were subject to this Commission's January 1, 1997 deadline.

local facilities network efficiently to CLECs is stunted by the fact that, in doing so, the RBOC's retail operations will lose customers and revenue. 3/

This petition of LCI, together with the companion petitions filed by LCI in New York and Illinois, present a way to break the logiam and jump-start more active retail -- and especially residential -- competition by creating a path (herein called "Fast Track") by which RBOCs voluntarily can reduce these conflicts of interest. Specifically, LCI proposes a corporate structure that would separate the retail and wholesale activities of the RBOC Holding Company ("HoldCo") into two separate subsidiaries. The retail company ("ServeCo") would have substantial public ownership and independent management. ServeCo would interact with the wholesale company ("NetCo") on the same arm's length, non-discriminatory basis, as any other retail service provider.



RBOCs choosing this voluntary, alternative "Fast Track" would be able to enter the interLATA market more quickly based on rebuttable presumptions of Section 271 compliance. And

<sup>3/</sup> These problems have implications both before and after interLATA entry. Today, the impediments to local competition are preventing the RBOCs from meeting the conditions for interLATA entry specified in Section 271. But even after a Section 271 petition is approved, under the current framework these same conflicts of interest will remain and hence, absent signified structural separation, the FCC and state commissions will need to engage in significant regulation to ensure that the RBOCs do not use their monopoly control of the only ubiquitous wireline network to perpetuate their retail services monopoly.

thereafter ServeCo would be regulated like a Competitive Local Exchange Carrier ("CLEC"), without the restrictions and level of oversight that otherwise would be necessary.

This proposal is fully consistent with the Act (indeed, none of the requirements or standards of the Act are altered in any way). It also preserves the central role of the states in supervising local telecommunications. LCI is filing related petitions with the Illinois Commerce Commission ("ICC") and the New York Public Service Commission ("NYPSC") asking them to open their own proceedings to implement the "Fast Track" approach. We encourage other states to do so as well. In that regard, we note that the LCI plan does not limit the ability of the states to take other actions to promote local competition, or to protect their consumers with measures suited to their local situation.

Such proceedings already are necessary in the states. Existing state regulatory policies will need revision to accommodate the watershed event of interLATA RBOC entry. Moreover, states will need to consider additional measures to break down barriers to residential competition. LCI is asking the ICC and the NYPSC -- and by extension all states -- to recognize that residential competition can be fostered, and post-271 regulation can be much less extensive, if RBOC retail and wholesale operations are structured independently as we propose. Consistent with our desire to break the current stalemate quickly, we are asking the ICC and the NYPSC immediately to open proceedings to: (a) consider the intrastate changes necessary to implement the LCI separation plan, (b) investigate how RBOC interLATA entry will impact, and require modification of, existing regulatory processes, and (c) explore additional actions that can reduce barriers to residential competition. 4/ These proceedings are similar to those under way in many states to promote competition in the electric utility industry.

<sup>4/</sup> LCI is filing petitions in New York and Illinois because these two states were among the first to begin the process of attempting to create local telephone competition. However, we fully recognize the major efforts of many other state commissions to create meaningful local competition, and encourage them to pursue the same solution to the current stalemate.

If adopted, the LCI "Fast Track" proposal would promote vigorous retail competition by all telecommunications providers, across all telecommunications services, for residential as well as business customers, in all areas of the country, with the least regulation possible—and would do so quickly. Indeed, if adopted, it is reasonable to believe that fully open and unrestricted retail residential and commercial competition could begin in some states by the end of 1998. By this we mean both local service competition from companies such as LCI, and interLATA service by the RBOCs.

These matters are discussed fully below. LCI explains the conflicts of interest that create the current stalemate. We present our detailed plan to reduce those conflicts in a way that would permit expedited interLATA authorizations and reduced RBOC regulation thereafter. We demonstrate the many benefits of the "Fast Track" approach, and its full consistency with the Communications Act, including the 1996 Telecom Act. Finally, we summarize how the key role of the states is preserved and enhanced by this plan. We urge the Commission to move swiftly to grant the declaratory rulings necessary to implement "Fast Track," and thereby bring the benefits of competition to local residential consumers.

#### I. THE SOURCES OF STALEMATE.

#### A. Three Critical Barriers.

Section 251(c)(3) imposes an express set of obligations on RBOCs to open their networks to other providers on non-discriminatory terms. Congress recognized that local telephone competitors could not offer adequate service without using the ubiquitous RBOC network on the same terms enjoyed by the RBOC itself. 5/ The Act thus required RBOCs to take on this wholesale "carrier's carrier" function.

<sup>5/ 47</sup> U.S.C. § 251(c)(3); Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, First Report and Order, CC Docket 96-98, 11 FCC Rcd 15499, 15510, paras. 14-15 (1996) ("Local Competition Order"), aff'd in part and rev'd in part, sub nom. Competitive Telecommunications Ass'n v. FCC, 117 F.3d 1068 (8th Cir. 1997); Iowa

In practice, however, the mandate of the Act remains unfulfilled. The lack of RBOC compliance with Section 251 has prevented full scale local competition, especially in the residential market. A brief summary of three critical barriers raised by RBOCs to date provides a key to understanding how they would be resolved through LCI's proposal.

#### 1. The OSS Barrier.

The FCC recognized in its *Local Competition Order* that nondiscriminatory access to operations support systems was "vital to creating opportunities for meaningful competition," and that it was an "absolutely necessary" prerequisite to full-scale competition in the local market. 6/
The Commission established a January 1, 1997 deadline for RBOCs to meet this requirement, 7/
but none has done so even a year later. As the Commission well knows, LCI has a petition pending in which we demonstrate overwhelmingly the need for OSS performance standards, measurements, and remedial provisions. 8/ LCI continues to urge immediate Commission action on that petition.

The fundamental problem in OSS parity is that the RBOCs use internal, well-established OSS to provision their own customers, while CLEC competitors must use new, fragile, slow and

Util. Bd. v. FCC, as amended on rehearing Oct. 14, 1997, 120 F.3d 753 (8th Cir. 1997), cert. pending, citing Conference Report at 121.

<sup>6/</sup> Local Competition Order, 11 FCC Rcd at 15764, 15766, paras. 518, 521, 523.

Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Second Order on Reconsideration, CC Docket 96-98, 11 FCC Rcd 19738, 19742-44, para. 9 (1996).

See Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Docket No. 96-98, Petition for Expedited Rulemaking of LCI and the Competitive Telecommunications Association (filed May 30, 1997) ("LCI Petition"). The LCI Petition set out the extensive evidence of the problems faced by CLECs in obtaining nondiscriminatory access to OSS, including: excessive manual intervention; lack of standard processes and interfaces; significant delays in processing customer orders and providing billing information; and substantial limitations in systems for maintenance and repair. These problems were confirmed by and expanded on through the more than fifty filings by other CLECs, state commissions and users.

still largely manual OSS interfaces. The difficulty in measuring "parity" between two wholly different and fundamentally unequal systems is what drives the need for the most detailed and extensive performance standards. Until such standards are adopted and met, measuring "parity" will continue to involve largely swapping horror stories about OSS.

Furthermore, the current OSS issues threaten to be just the tip of the iceberg. Today's problem is to get some kind of satisfactory order processing system in place. But in the future the discrimination problem will become more subtle. The Commission will need to be sure that order processing continues to be equivalent for the retail operations of both the RBOCs and competitors. But the Commission also will face new issues related to billing information, maintenance and repair, and other "customer care" activities central to the wholesale function. Thus, RBOC incentives for anticompetitive discrimination will not go away, while opportunities to discriminate will expand exponentially beyond the specific OSS issues being debated today.

#### 2. The UNE Barrier.

A second source of stalemate has been the unwillingness of RBOCs to provide UNEs in the manner requested by the CLECs, and on the same terms as they provision their own retail operations. Given LCI's large residential customer focus, we have been particularly frustrated by the RBOCs' response to requests for the so-called network element "platform" configuration. It is widely accepted (at least outside the RBOC community) that the ability to use UNEs efficiently in combination is crucial to widespread local service competition, especially for residential consumers.

The FCC has found 9/, and the Eighth Circuit affirmed 10/, that requesting carriers have the right to purchase all of the UNEs needed to provide local service, and to operate them in a

<sup>2/</sup> Local Competition Order at 15666-71; paras. 328-41; accord Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges, First Report and Order, 7 C.R. 1209, FCC 97-158, CC Docket Nos. 96-262, 94-1, 91-213, 95-72 (rel. May 16, 1997), at paras. 32, 337 ("Access Charge Reform Order"), modified in other respects Errata (rel. June 4, 1997); Order on Reconsideration, 12 FCC Rcd 10119 (1997); Second Order on Reconsideration and Memorandum Opinion and Order, FCC 97-368, CC Docket Nos. 96-262, 94-1, 91-213 (rel. Oct.

platform configuration. The remaining issue is whether the RBOCs will prevent efficient platform-based competition pursuant to Section 251. Here, the stalemate is most obvious. RBOCs are not only refusing to "do the combining" on cost-based terms, but also announcing that they will "uncombine" preexisting element configurations serving a customer location when that customer selects an alternative local service provider. RBOCs are artificially insisting that when competitors order network elements, those elements must be physically disconnected and then reconnected by the CLEC, creating unnecessary costs and delays, and substantially increasing the risk of service outages. For example, some RBOCs are proposing to require CLECs to go to the unnecessary expense of collocating in every central office in which they seek to combine network elements. 11/ Significantly, the RBOCs are imposing these costs and burdens only on their competitors; the same disruptive processes will not apply to their own retail services.

LCI submits that these RBOC activities violate the requirements of Section 251, which clearly prohibit ILECs from interfering with the CLECs' ability to combine elements efficiently themselves, and which guarantees CLECs non-discriminatory access to the RBOC facilities to do so. 12/ For present purposes, however, what is relevant is that the RBOCs are not voluntarily

<sup>9, 1997);</sup> petitions for review pending sub nom. Southwestern Bell Tel. Co. v. FCC, No. 97-2618 (and consolidated cases) (8th Cir., filed June 16, 1997).

<sup>10/</sup> Iowa Utilities Bd., 120 F.3d at 813.

<sup>11/</sup> See, e.g., Application of BellSouth Corp. Pursuant to Section 271, CC Docket No. 97-208, FCC 97-418 (rel. Dec. 24, 1997) at para. 190 (BellSouth requirement that a CLEC employ collocation in order to combine loops and switching); "Bell Atlantic-New York Product Offerings: A Guide to Enabling Competitive Local Exchange Carriers to Combine Unbundled Network Elements," Nov. 13, 1997 (Bell Atlantic requirement that CLECs establish a physical presence in the central office to connect elements there). Compounding the problem is Ameritech's refusal (and perhaps the refusal of other RBOCs) to provide shared transport, even after the FCC affirmed its conclusion that shared transport was an unbundled element that must be provided under Section 251(c)(3).

<sup>12/</sup> Unfortunately, the Eighth Circuit has held that ILECs are not required to provide access to existing element combinations. LCI believes that the Eighth Circuit's decision was wrong and

acting like vendors in a competitive market. The RBOCs are refusing to give the CLECs what those carriers say they need to provide local service -- especially to residential customers: the ability to use cost-based network elements in a connected form to quickly and reliably convert and then service customer locations (selling those end users their local service, and selling other carriers exchange access and termination to such end users).

Pointedly, it is useful to consider how different the RBOCs' actions are from those one would expect if their primary focus were to provide local network elements, and if they did so in competition with other network vendors. In that event, the negotiation process contemplated by Section 252 almost certainly would work much more smoothly. An independent wholesale vendor has incentives to negotiate fairly with its customer, and to resolve contractual issues quickly on a "win-win" basis so that the vendor can sell its wholesale product, and the customer can use that product in its business. Section 252 was intended to create that market dynamic, with an arbitration process as a safety net. But the enormous number of disputes over interconnection clearly demonstrate that the 252 negotiation process is not working as intended.

Similarly, if the RBOCs' primary function were to provide network elements, and if they faced competition in that role, the RBOCs could be expected to go out of their way to meet carrier-customer requests. In such a world, the RBOCs would not be taking the step of artificially breaking up existing configurations to force their carrier-customers to put them back together. 13/ Rather, the RBOCs would be trying to help their carrier-customers by selling

will be reversed by the Supreme Court. But the UNE stalemate will not end when the Supreme Court rules on this issue. RBOCs still will have a continuing incentive to find ways to discriminate in the provision of UNEs to their retail service competitors. If the Court reverses, RBOCs may acknowledge their obligation to combine elements (and just as importantly, the prohibition on disrupting elements that already are combined), yet still refuse to do so efficiently for their competitors. If the Court agrees that CLECs must do the combining, RBOCs likely will continue to impose barriers that make this legal option impossible in practice. Either way, the result would be the same: competing carriers would be denied efficient use of UNEs in the form they require.

<sup>13/</sup> In complete contrast, when the RBOCs go to satisfy their interLATA network requirements, they meet no similar obstacles. Quite the contrary, in their competition to get the

existing combinations where requested, and by voluntarily combining elements to create new configurations upon request. Today, however, RBOCs reserve this treatment for themselves, and meet the business needs of their competitors only to the extent that regulators eventually force them to do so.

## 3. The Pricing Barrier.

Sections 251 and 252 of the Act require the RBOCs to price at cost and on a nondiscriminatory basis. 14/ There is a substantial overlap between these obligations -- and enforcement of these obligations -- in an environment of mixed wholesale and retail operations. The only way to assure non-discrimination in the prices charged by the RBOC to its rivals is to assure that they are cost-based. Unfortunately, this process is difficult and complex at best, particularly in an environment where the RBOC has every incentive to hide discrimination in favor of its own retail services through, for example, inaccurate cost studies.

LCI strongly agrees that the RBOCs must be required to set their prices for UNEs and other network inputs at cost, that is, at TELRIC. Cost-based rates are critical both to permit competition to proceed over the ubiquitous RBOC network today, and to create conditions for efficient interconnection of competing network facilities as they are deployed. Only then will CLECs be using the RBOC network at rates equivalent to the internal cost of the RBOC to use those same inputs itself. Furthermore, only economically efficient network prices will provide the maximum benefits to consumers and send appropriate signals as to where, and when, companies should make facilities investments.

In addition, competition in the local market will be impossible if RBOCs are able to charge their retail competitors higher rates for wholesale inputs than the internal cost reflected in the RBOCs' own retail operations. This is true whether the discrimination comes in the form of

RBOCs' business, operators of interLATA networks compete vigorously to offer both lower prices and the network configurations that the RBOCs desire.

<sup>14/</sup> See 47 U.S.C. § 252(d).

excessive rates for competitors to use UNEs, excessive non-recurring UNE charges, or excessive charges for any other local network activity such as maintenance or order processing. The same would also be true if the RBOCs are able to subsidize their retail offerings with monopoly rents from the provision of facilities and service to competing carriers.

Unfortunately, the pricing issues that have arisen are complex, contentious, and appear destined never to end. RBOCs are litigating cost standards to be used in this process, but even after a standard is developed, 15/ huge resources still will be necessary to evaluate RBOC prices and enforce non-discrimination principles. Without such regulation, the RBOCs will have the power to thwart competition intended by the Act. But LCI's "Fast Track" plan should substantially lessen the level of scrutiny required.

## B. The Common Thread in the Barriers: Inherent Conflicts of Interest.

A common thread links these and other barriers to local competition -- RBOC conflict of interest. An RBOC has two conflicting roles: (i) operator of the local wireline network that all carriers rely upon to provide retail services; and (ii) competitor in the retail market itself. Thus, whatever incentive an RBOC has to fulfill its statutory obligations to open its network, it has an equally strong, if not far stronger, incentive to prevent retail competitors from capturing local market share. 16/

As the Department of Justice recognized, this absence of a consistently applied costing methodology creates great uncertainty regarding future prices, and hence "it is not surprising that there is no real competition using unbundled elements now, or that competitors' plans to compete in the future are subject to many contingencies." See DOJ SC Evaluation at 40-41.

<sup>16/</sup> Thus, the requirements of the Act are "counterintuitive" from the perspective of the RBOCs, as was recently observed by Joel Klein, Assistant Attorney General for Antitrust of the United States Department of Justice. Klein noted that RBOCs must be held to "tough performance measures" under Section 271 because it was "counterintuitive" for them to open their networks to allow CLECs to compete with them and capture market share. See Communications Daily, at 2 (Dec. 12, 1997).

This inherent conflict of interest lies at the center of the problems the industry is facing in bringing local competition to consumers -- especially in the residential market. Congress recognized the problem and attempted to deal with it. Sections 271 and 272, in addition to 251(c), established specific obligations on RBOCs to make their networks available to other carriers because Congress saw that the RBOCs had no incentive to do so voluntarily. 17/

Unfortunately, however, the Commission and the states have faced huge difficulties in attempting to enforce these clear RBOC obligations -- despite the fact that today the RBOCs have the special, one-time, incentive of Section 271 interLATA entry. After such entry, regulators will be forced to monitor RBOC activity even more closely, at great expense and burden, to ensure that RBOCs do not use their control of the local network for anti-competitive ends. But the prospect of permanent regulatory vigilance only promises unending state and federal regulatory proceedings. If such regulation fails, then telecommunications consumers could find themselves doubly cursed. They could lose both their best chance for local service competition, and also the long distance competition they already enjoy.

### II. LCI'S "FAST TRACK" PROPOSAL.

LCI believes the Act can work as intended, and soon -- provided that this Commission and the states adopt an alternative "Fast Track" approach to regulation that meaningfully addresses the RBOCs' inherent conflicts of interest. "Fast Track" is based on a tool that is available under the Act, and often used by the Commission in analogous circumstances—structural separation. LCI believes that adequate structural separation between an RBOC's

<sup>17/</sup> This Commission has recognized this conflict expressly in its Non-Accounting Safeguards Order: "For example, a BOC may have an incentive to degrade services and facilities furnished to its affiliate's rivals, in order to deprive those rivals of efficiencies that its affiliate enjoys. Moreover, ... a BOC that discriminates against the rivals of its affiliates could entrench its position in local markets by making these rivals' offerings less attractive. ... Moreover, if a BOC charges other firms prices for inputs that are higher than the prices charged, or effectively charged, to the BOC's section 272 affiliate, then the BOC could create a 'price squeeze.' Non-Accounting Safeguards Order, supra, 11 FCC Rcd at 21912, para. 11.

wholesale network operations and its retail affiliate would substantially lessen the conflicts inherent when the RBOC provides inputs to competitors while competing directly with them. It therefore would simplify the process of Section 271 interLATA entry. Separation also would make reliance on post-entry regulation to control RBOC behavior less important, and therefore less intrusive, complicated, and time-consuming for all involved—the FCC, the state commissions, the RBOCs, and CLECs.

We emphasize that the "Fast Track" proposal differs fundamentally from ILEC-designed retail/wholesale separation plans (including the plans that have been implemented by Rochester Telephone ("Rochester") and Southern New England Telephone ("SNET"). These ILEC plans do not go nearly far enough to cure the conflicts of interest at the root of the current stalemate. Furthermore, the RBOCs raise competitive issues that are far more serious than those presented by smaller, geographically constrained, independent ILECs.

LCI calls its proposal "Fast Track" because it promises to achieve real local competition
-- for residential as well as business consumers -- on a rapid basis. This in turn means that
RBOC interLATA entry also could be accelerated safely.

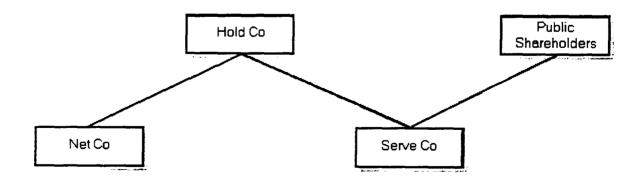
It is important to note, however, that all elements of the proposal must be implemented for the RBOCs' inherent conflicts of interest to be checked sufficiently. Any watering down of the minimum requirements of the plan would undo the safeguards justifying 271 entry and reduced RBOC regulation. At the same time, the "Fast Track" plan preserves the traditional ability and jurisdiction of state commissions to take any other actions to promote local competition, or to protect their consumers, as part of their own consideration of these issues. With these caveats, the details of the proposal are as follows:

## A. The Substance of the Proposal.

## 1. The Proposal in General.

LCI proposes that the Commission adopt an optional "Fast Track" path which the RBOCs may, but are not required to, employ. Specifically, LCI proposes that the Commission set forth a wholesale/retail corporate structure that, if implemented by an RBOC, could justify a rebuttable presumption of compliance with Section 271 and obtain reduced regulation rapidly. The RBOCs would separate completely their retail and wholesale activities. The RBOC holding company ("HoldCo") would establish a retail service company ("ServeCo") separate from its existing local network operations ("NetCo"). Under this plan, the RBOC would remain a telecommunications provider fully subject to all provisions of the Act. The RBOC's retail local and long distance telecommunications service activities would be housed in ServeCo, while NetCo would manage the local network and sell it on a "carrier's carrier" basis to all retailers, including ServeCo, interfacing with every retail service provider on the same basis using the same personnel and systems.

Importantly, ServeCo would have incentives and fiduciary duties separate from HoldCo and NetCo. ServeCo would have partial public ownership independent of HoldCo, independent directors representing the public shareholders, and independent management compensated entirely based on ServeCo's financial performance.



All new retail customers would be provided service through ServeCo or other CLECs. On a transitional basis, NetCo would continue to serve the existing RBOC local customer base. However, NetCo would not be permitted to add customers, nor would it be permitted to add new retail services or actively market retail services to that base. ServeCo would have to compete for, win over, and assume all retail responsibility for a NetCo local customer in competition with other CLECs in order to provide that customer with interLATA long distance. NetCo thus would lose its retail local subscribers over time to ServeCo and others. State commissions could decide whether and at what point it is appropriate to transition all residual local customers out of NetCo through balloting and allocation, making NetCo a "pure" wholesale company.

The "Fast Track" proposal is fundamentally different from any of the retail/wholesale plans that have been implemented or proposed by ILECs. The SNET plan, for example, provides for the eventual elimination of the network company's retail activities, but it does not require the retail company to use the same OSS that CLECs must use. 18/ The SNET plan also does not provide for public ownership or other indicia of independence in the retail company, nor does it require full separation of the two companies. The Rochester plan suffers from these same defects, and in addition, does not require that the retail base of the network company ever be competed or balloted away. 19/ GTE and BellSouth, among other ILECs, have sought authority

<sup>18/</sup> DPUC Investigation of the Southern New England Telephone Co. Affiliate Matters Associated with the Implementation of Public Act 94-83, Decision, Docket No. 94-10-05 (CT Dept. of Pub. Util. Control June 25, 1997) ("SNET Affiliate Initial Decision"), modified by Decisions dated Sep. 10, 1997; Oct. 8, 1997; Oct. 28, 1997; and Dec. 22, 1997. The SNET plan also provided for balloting and allocation to begin shortly after the restructure took place. The Connecticut DPUC recently ordered that balloting be moved back by at least a year, citing inadequacies in the OSS systems for both SNET and the CLECs. SNET Affiliate Decision Delaying Elements of the Transition (Dec. 22, 1997) at 2, 5-6. The DPUC also required that balloting not take place until SNET had demonstrated parity between the OSS systems used by its retail affiliate and those used by CLECs. Id.

<sup>19/</sup> Petition of Rochester Telephone Corp. for Approval of Proposed Restructuring Plan, Opinion and Order Approving Joint Stipulation and Agreement, Case Nos. 93-C-0103, 93-C-0033, Opinion No. 94-25 (NY Pub. Serv. Comm'n. Nov. 10, 1994) ("Rochester Order;" "Rochester Joint Stipulation and Agreement").

to offer local exchange services in competition with their own network company in their service areas, but these proposals offer nothing to ensure that the ILEC's CLEC affiliate will be independent from the ILEC. In fact, all these proposals are simply thinly disguised attempts to move selected local exchange retail activity into an unregulated subsidiary (exempt, they claim from Section 251(c) obligations that otherwise would apply). These ILEC plans do nothing to address the core incentives and ability of the parent holding company to manipulate the subsidiaries in ways that discriminate against CLECs. 20/

In short, the mere separation of retail and wholesale activity does not cure the ILECs' underlying conflicts of interest. 21/ In the sections that follow, LCI first sets forth the specific details of its proposal which address these conflicts. We then explain how these elements collectively satisfy the seven minimum criteria for adequate separation of RBOC wholesale and

<sup>20/</sup> See, e.g., Application of GTE Communications Corp. for a Certificate of Operating Authority in SWBT, Sprint/United and Centel Service Territories, Order, Docket No. 18146 (TX Pub. Util. Comm'n Oct. 30, 1997) ("GTE CLEC Certification Order") (denying GTE a CLEC certificate in its local service area); Application for Certificate to Provide Alternative Local Exchange Telecommunications Service by BellSouth BSE, Inc., Order Granting Certificate, Docket No. 971056-TX, Order No. PSC-97-1347-FOF-WS (FL Pub. Serv. Comm'n Issued Oct. 27, 1997) ("FL BellSouth Certification Order"), petitions for administrative hearing granted (Order Establishing Procedure, Jan. 14, 1998) (setting BellSouth's CLEC application for hearing); Application of BellSouth BSE, Inc. for Certificate of Public Convenience and Necessity to Provide Local Exchange Services in the State of South Carolina, Order Approving Certificate, December 23, 1997 (granting BellSouth's CLEC certificate). Opponents to these proposals have correctly argued that simply moving an ILEC's retail activities into a separate affiliate is not a basis for exempting those activities from Section 251(c) and other requirements applicable to incumbent LECs.

LCI's plan also differs from the Section 272 model for the separate interLATA affiliate because it goes beyond Section 272 in that the RBOCs would voluntarily agree that *all* retail services will be provided through that affiliate (except for the embedded base) and because it gives that affiliate other indicia of true independence (such as outside public ownership and management compensation tied solely to the affiliate's performance). Unlike the Section 272 affiliate, ServeCo would have incentives to act as if it were an independent CLEC, and not just another self-dealing arm of the RBOC.

retail activity. Because the "Fast Track" plan contains all the "seven minimums," it would unlock the door to residential local competition and Section 271 entry. 22/

## 2. LCI's Proposal in Detail.

## a. The Corporate Structure.

- (i) Separation of NetCo from ServeCo would be absolute, other than the parent HoldCo's partial ownership in ServeCo. ServeCo would not share officers, directors, personnel, equipment, buildings, services, or other resources with HoldCo or NetCo (or any affiliate of those entities).
- (ii) ServeCo would have sufficient minority public ownership (in the range of 40% or more) to ensure that it has a significant fiduciary obligation other than to HoldCo. Because its shares would be owned and publicly traded by persons or institutions expecting to earn profits from ServeCo's operations without regard to ServeCo's affiliation with HoldCo or NetCo, market pressures would help give the retail affiliate stronger incentives to earn a reasonable return on investments. ServeCo also would have independent reporting requirements under the securities laws, and would be subject to suits from its public shareholders if operated in a way that unduly advantages HoldCo (or any of HoldCo's affiliates, including NetCo).
- (iii) ServeCo would have independent board members specifically charged with representing the interests of the public shareholders. 23/

<sup>22/</sup> At the same time, the "Fast Track" plan preserves the ability of state commissions to take other actions to promote local competition or to protect their consumers with measures particularly suited to their local situations.

<sup>23/</sup> By "independent director" we mean a director who has no financial interest in NetCo or HoldCo (including stock ownership), has no employment or consultant relationship (past or present) with NetCo, HoldCo, or any other HoldCo affiliate, and has no other present or past business or professional relationship with NetCo, HoldCo, or any HoldCo affiliate that could affect her independent judgment.

- (iv) Compensation of ServeCo management (including bonuses and stock options) would be tied only to the financial success of ServeCo, not to the success of HoldCo (or any other HoldCo affiliate). Stock options would be awarded only in ServeCo stock.
- (v) Section 272 separation requirements would apply, including FCC-prescribed accounting and non-accounting safeguards. 24/

#### b. Role of NetCo.

- (i) NetCo would own and operate the existing RBOC local exchange network, and would be required to make that network and related operational support available equally to ServeCo and all CLECs. 25/
- (ii) NetCo's embedded base of customers would be assigned to competing CLECs (including ServeCo) through balloting and allocation at a time to be determined by state utility commissions.
- (iii) To avoid disruption to the embedded base of existing local customers, NetCo would continue to provide them with retail local exchange and intraLATA telephone service during the transition period prior to balloting. However, NetCo could not accept any new customers (including existing customers who physically move within the local area).

<sup>24/</sup> These requirements would apply to transactions and other arrangements between ServeCo and either HoldCo, NetCo or their affiliates.

<sup>25/</sup> NetCo shall retain all facilities, systems, information, licenses, other intellectual property rights, and other assets used in connection with, or otherwise relating to, the provision of interconnection, network elements, and exchange, exchange access, and intraLATA toll telecommunications services, including all pre-ordering, ordering, provisioning, maintenance and repair, billing and collection, and other operations support system, customer care, and associated functions. None of these assets and capabilities would be transferred upon restructure to ServeCo. To the extent NetCo thereafter provides these assets and capabilities to ServeCo, it would do so only on the same terms and conditions upon which the assets and capabilities are made available to any other carrier.

- (iv) NetCo's retail tariff would be frozen. Existing NetCo customers would be able to add a feature from the tariff in effect at the date of implementation. However, new retail products would be provided by ServeCo, not NetCo.
- (v) NetCo would be precluded from engaging in any retail marketing, even to its embedded base of local exchange customers or to others.
- (vi) NetCo would provide interconnection and network elements, as well as meet the other obligations of Sections 251 and 252. During the transition period prior to allocation, NetCo also would provide wholesale versions of its retail local and intraLATA telecommunications services for resale, and exchange access to CLECs needing to reach the existing customer base.
- (vii) NetCo would be obligated to provide combinations of network elements on a prompt and efficient basis reflective of its actual cost. NetCo would be prohibited from disrupting network element combinations, except at the request of the CLEC.
- (viii) NetCo could expand and enhance the local network as it deemed appropriate in its business judgment, and on a non-discriminatory basis, to meet the needs of carrier-customers, including ServeCo.
- (ix) NetCo would be precluded from transferring local network facilities to ServeCo.

#### c. Role of ServeCo.

- (i) ServeCo would be allowed to offer all the services of a CLEC. Thus, ServeCo could offer any retail service to any end user. ServeCo also would offer exchange access and interconnection to other carriers who need to originate or terminate traffic to a ServeCo end user.
- (ii) During the transition period prior to balloting and allocation, ServeCo would not be allowed to provide interLATA service to NetCo customers until and

unless NetCo's OSS systems to provision and support network element combinations are capable of processing the same volumes of customer transfers, at the same intervals, as the PIC-change systems used to process long distance customer transfers. 26/ No other restrictions would apply to ServeCo's retail operations. Thus, ServeCo could sell both local and interLATA service to NetCo customers, in which event their local service would be switched to ServeCo using the same OSS and carrier's carrier network offerings as used by other CLECs. ServeCo also could sell stand-alone interLATA service to any customers previously switched to another CLEC.

- (iii) ServeCo would be the Section 272 interLATA affiliate. Unless it met the same level of separation, no other RBOC affiliate could provide retail local exchange service or interLATA services.
- (iv) ServeCo would not bear the obligations of an ILEC under Sections 251 and 252, though these obligations would continue to apply to HoldCo and its wholly-owned subsidiary, NetCo (as well as successors and assigns of those entities).
- (v) ServeCo would be free to buy network inputs from other carriers besides NetCo. It also could build its own network, just as other CLECs may.

### d. Nondiscrimination.

(i) ServeCo would interface with NetCo in exactly the <u>same</u> manner as other CLECs do. ServeCo would need to switch every local customer that it wins from NetCo, just as any other CLEC would, using the same OSS interfaces, and would purchase wholesale inputs from NetCo at the same rates, terms, and conditions as

<sup>26/</sup> This transitional restriction would erode in relevance as NetCo loses customers in the ordinary course, and would disappear once OSS systems supporting network element combinations are comparable to the PIC-change process.

other CLECs. NetCo would not be permitted to develop or use any interfaces or OSS equipment with ServeCo that are not also available to other CLECs.

- (ii) NetCo could not treat ServeCo any differently than any other CLEC (e.g., no endorsement or other recommendation of ServeCo; no transfer of customer calls to ServeCo unless pursuant to identical and nondiscriminatory terms, conditions, procedures and practices that would apply for every other carrier, etc.). NetCo also would have to follow nondiscriminatory procedures for handling inquiries from its embedded customer base regarding available providers for local, long distance, or other service, without mentioning its affiliate except as part of a larger random list.
- (iii) NetCo may provide wholesale facilities and services to ServeCo only under published tariffs. If interconnection agreements are entered into between ServeCo and NetCo, they must be documented in tariffs and subject to a "pick-and-choose" rule. 27/
- (iv) ServeCo may have access to and use information about NetCo's customers only pursuant to the FCC's CPNI regulations, and only if other carriers can obtain the same information on the same terms and conditions. ServeCo may not take with it any such information, or other ILEC asset, upon separation.
- (v) To avoid customer confusion, NetCo and ServeCo must operate under materially different trade names and service marks that do not reflect any affiliation. For example, HoldCo may allow either NetCo or ServeCo to use HoldCo's name, but not both.

We recognize that the FCC may not currently be able to order "pick-and-choose." Rather, this would be a necessary condition of our voluntary structural separation proposal.

## e. Balloting and Allocation.

- (i) Over time, residential and commercial retail customers of NetCo would migrate to ServeCo or to its CLEC competitors. When the relevant state commission determines that wholesale OSS systems to provision and support network element combinations are capable of processing the same volumes of customer transfers, in the same intervals as the PIC-change systems used to process long distance customer transfers then a state commission would be free to order balloting to remove the remaining retail customers from NetCo. 28/ At that point, NetCo would be a pure "carrier's-carrier."
- (ii) Any non-balloted customers would be allocated among ServeCo and its CLEC competitors on a competitively neutral basis. Allocation procedures would need to be approved by the state commissions

## f. Regulation of the Companies.

- (i) All NetCo offerings purchased by ServeCo would be via tariff (or some other generally available mechanism), with prices established by the state commissions subject to the requirements of Section 252(d). The interconnection agreements between NetCo and CLECs would continue in force, with general nondiscrimination requirements applying.
- (ii) ServeCo's retail services would be regulated on the same basis as the those of its CLEC competitors. As a general rule, bundling of all retail services would be allowed and rates for all retail services and service packages would be subject to limited or no regulation. If deemed necessary after NetCo exits the retail market following balloting/allocation, state commissions could require all retail

<sup>28/</sup> This would provide the public time to become familiar with the presence of local competitors.

companies to offer a "basic" no-frills local exchange service offering at an affordable rate as a precondition to universal service support.

- (iii) Access rates of ServeCo would be regulated no differently than the access rates of its CLEC competitors (for example, they could be subject to a cap on terminating access rates, if one applied to other CLECs).
- (iv) NetCo could offer access only in connection with its embedded customer base. Exchange access rates of NetCo would be regulated the same way they are today, under the interstate price cap rules and whatever state regulation applies to intrastate access.
- (v) NetCo would be regulated as the incumbent ILEC, including pursuant to Sections 251 and 252.
- (vi) NetCo could not provide non-cost-based discounts volume or other types) to ServeCo or any other carrier.

## g. Universal Service Support.

- (i) ServeCo would be eligible for universal service funding in connection with its purchase of network elements to the same extent as any other retail service provider.
- (ii) NetCo would receive universal service funding to the extent it continues to serve retail local exchange customers.
- (iii) After balloting and allocation, as before, state commissions would ensure that the network element rates are cost-based and therefore sufficient to ensure NetCo's financial integrity.
- (iv) States remain free to adopt other non-discriminatory measures to protect universal service.

#### h. Sunset.

(i) The ServeCo/NetCo structure would remain in place once implemented.

nondiscrimination in the provision of wholesale inputs by NetCo, crucial elements of the Act's interLATA preconditions. 31/

- (ii) Section 251(h). The FCC would declare that, when an RBOC elects to operate on this partially separated basis, ServeCo will not be considered a "successor or assign" or ILEC "replacement" for purposes of Section 251(h), and therefore will not be subject to those Section 251(c) obligations. This conclusion is justified because the independence of a ServeCo constituted as described herein, and the continuing obligations of NetCo, together reduce the concerns embodied in Section 251(h) that an RBOC might sidestep its duties under the Act through new corporate affiliates.
- (iii) ServeCo Regulation. The FCC would declare that a properly constituted ServeCo will be considered a non-dominant carrier for all purposes, and therefore subject to the same regulation as other CLECs. This ruling would allow ServeCo to bundle packages of local and long distance, and provide exchange access, on a non-dominant basis, as well as be excused from other regulation. This conclusion is appropriate because the incentives and ability of NetCo to discriminate in favor of ServeCo are reduced by the structural changes the FCC would require in its rulings.

Importantly, we are not asking the Commission to require any RBOC to make the corporate structure changes needed to qualify under this "fast track" approach. Instead, we are suggesting that the FCC make this "fast track" approach available for any RBOC wishing to so qualify. 32/

<sup>31/</sup> The RBOCs still would need to meet the prerequisites of Section 271(c)(1)(A) or (B) (the "Track A" or "Track B" tests).

<sup>32/</sup> Furthermore, we are asking that the FCC establish this alternative to be available in any instance where a state commission orders this structure to achieve its own regulatory objectives.

- (ii) HoldCo could not opt out of the plan after entering the interLATA market through ServeCo.
- (iii) At the point when CLECs no longer are dependent on the RBOC wireline network because competitive alternative local exchange networks have developed, 29/ the FCC and state commissions may revise their policies and rules in ways that would permit NetCo and ServeCo to merge, or permit NetCo to enter the retail market by other means, including a transaction with a retail service provider other than ServeCo.

## B. Steps to Be Taken by the FCC.

The Commission can clear the path to this "Fast Track" Section 271 option through a few, relatively simple declaratory rulings. They are as follows:

(i) Section 271. The FCC would declare that, if an RBOC creates a ServeCo satisfying the key elements of separation and independence set forth here, the RBOC will receive a rebuttable presumption that it has met the competitive checklist and public interest test of Section 271. 30/ This presumption is justified because the change in the RBOC's incentive structure and separation that would result from the creation of ServeCo sufficiently improves prospects for parity and

<sup>29/</sup> The FCC and state commissions would have to determine that actual, market-disciplining facilities competition exists throughout the RBOC's region.

<sup>30/</sup> The RBOC also must actually be providing or generally offering each checklist item in order to meet Section 271. 47 U.S.C. § 271(c)(2)(B). We recognize that under this proposal, the ultimate burden of proof still rests with the RBOC. See Application of Bell South Corp. Pursuant to Section 271, CC Docket No. 97-208, FCC 97-418 (rel. Dec. 24, 1998) at para. 37. However, the rebuttable presumption should substantially expedite the process by which an RBOC meets that burden.

As importantly, LCI is not suggesting any alteration to the statutorily imposed Section 271 burden on the RBOCs, nor any lowering of standards or elimination of any competitive checklist item under Section 271. At the same time, however, qualification under Section 271 would be attainable much faster by an RBOC under this structure, and would be far easier for the Commission to determine and verify. For example, the competitive checklist provisions of Section 271 are designed to ensure that an RBOC makes available to retail competitors the tools necessary to provide local service, and in particular does so on a non-discriminatory basis. An RBOC retains an incentive to discriminate in favor of any affiliate. Nevertheless, if the RBOC is prepared to use exactly the same tools as CLECs, through an independent subsidiary, to provide its own retail local services, then it is more reasonable to presume that the checklist items will be provided on an effective and nondiscriminatory basis. Similarly, it is more reasonable to presume that in these circumstances, RBOC entry into the interLATA market now would be in the public interest.

This plan also is consistent with other sections of the Act, even as it permits substantially reduced regulation. For example, the obligations of Section 251(c) will continue, but enforcement will be simplified and focused on NetCo. Similarly, because discrimination concerns are reduced, the Commission and the states can adjust their regulatory policies accordingly for the post-entry period. Sections 201 and 202 will continue to apply to ServeCo's rates, but ServeCo's offerings will be presumed to comply with those sections (as are CLECs' offerings).

Properly understood, the proposal comports with what the Commission already has done in its *Non-Accounting Safeguards Order* under Section 272. Specifically, in that *Order* the Commission set out various rights and obligations of an RBOC affiliate under Section 272. 33/ The proposal here is fully consistent with those rights and obligations. Thus, the proposal simply says: If the RBOC is willing to go a step further in a manner that fundamentally alters its

<sup>33/</sup> Non-Accounting Safeguards Order, 11 FCC Rcd at 21913-15, 22054-58, paras. 14-19, 309-16.

incentives, then it will obtain additional benefits, which benefits ultimately would inure to consumers as well.

# C. Steps to Be Taken by the States.

The states also have a central role to play in making the proposal a reality, while addressing their own unique competitive and universal service goals. This petition, together with the related state petitions to be filed with this petition, address the states' role in this regard.

# D. Timing of Implementation of the Proposal.

If the Commission moves with expedition, LCI believes it would be feasible to adopt the necessary rulings by approximately June 30, 1998. State commissions could undertake similar proceedings under roughly the same schedule. Once approved, the RBOC-ServeCo affiliate could be implemented and prepared for unregulated retail competition within an additional four-to-six months after that. Hence, this proposal could produce open, unrestricted retail competition by the end of 1998 or soon thereafter.

# III. THE PROPOSAL HELPS TO RESOLVE THE MAJOR BARRIERS TO LOCAL COMPETITION.

# A. "Fast Track" Contains the "Seven Minimums" Needed to Address RBOC Conflicts of Interests.

LCI recognizes that, over time, various other parties have suggested separation of the RBOC's wholesale and retail operations -- to a greater or lesser degree -- as a means to resolve the conflicts of interest between them. 34/ More recently, as disputes over implementation of

<sup>34/</sup> See, e.g., Jerry Duvall, "The Evolution of Competition in the Market for Local Telecommunications Services: A Proposal for Industry Organization in the 21st Century," at 9, presented before the conference of the United States Telephone Association on "Survival Strategies for the Future: Planning for Change and Consolidation" (June 29, 1987)(proposing that LECs evolve toward an organizational structure where local exchange network facilities are operated in a corporate entity that remains subject to public utility regulation, and all retail local exchange services are provided over those facilities "by multiple, competing local Telecommunications Service Companies' that are completely unregulated.")

Section 251 have grown, one party has suggested that a new divestiture is necessary. Under this plan the RBOCs would be required to spin off their local network facilities to a wholly new company in which they have no financial interest at all. 35/

At the same time ILECs themselves, including the RBOCs, are recognizing the advantages of establishing separate retailing "CLEC" affiliates in which they hope to offer local and other services on an unregulated basis -- free from Section 251(c) obligations and retail rate regulation, for example. As noted above, these ILEC-designed plans typically contain serious competitive weaknesses that do not solve the conflict of interest problem underlying the current stalemate (and in fact, may make it worse). 36/

LCI is interested in breaking the current stalemate quickly so that it can realistically offer local service, especially to its residential customers. LCI's "Fast Track" proposal will not solve all regulatory issues. Nevertheless, we believe that this structure can advance consumer interests because it contains the seven minimum elements necessary to reduce RBOC conflicts of interest. We emphasize that the "seven minimums" are entirely indivisible; if one is missing the others are not effective. We further emphasize that "Fast Track" in no way interferes with the traditional jurisdiction of the states to take whatever additional steps they may deem necessary to enhance separation, prevent anti-competitive discrimination, and protect their consumers.

<sup>35/</sup> See, e.g., Letter to Reed E. Hundt, Chairman, FCC, from Roy L. Morris, US ONE, Aug. 11, 1997, filed in Recommendations for Commission Actions Critical to the Promotion of Efficient Local Exchange Competition, CCB Pol. 97-9, and Implementation of the Local Competition Provisions of the Telecommunications Act of 1966, CC Docket No. 96-98. Mr. Morris expands upon the LoopCo Plan in A Proposal to Promote Telephone Competition: The LoopCo Plan, CCH Power and Telecom Law, Vol.1, No.2 at 35 (January/February 1998).

<sup>36/</sup> In recognition of these problems, the Texas Commission denied GTE's request for CLEC authority in its own service area, and the Florida Commission is holding hearings on BellSouth's CLEC application. See GTE CLEC Certification Order, supra.; FL BellSouth CLEC Certification (Jan. 14, 1998 Order Establishing Procedure), supra.

## The "Seven Minimums" of Fast Track

- 1. NetCo and ServeCo would not share facilities, functions, services, employees or brand names. NetCo and ServeCo would be completely separate physically, operationally and functionally, and they would not share the same brand or trade name. Any sharing of resources would undercut the separation of corporate identities and strategic goals that is the foundation of this plan. It would raise cost allocation difficulties, and provide opportunities for joint activity abusing the relationship between the two affiliates. 37/
- 2. NetCo would not engage in any retail marketing. NetCo would shed its role as a retail company and focus on its task of providing wholesale network facilities to competing retail providers. This would provide the RBOC with the necessary incentives to make ServeCo a successful retail company.
- 3. ServeCo would deal with NetCo only on an equal (not "separate but equal") basis with other CLECs. Parity between the RBOC's provision of local exchange service to itself and to unaffiliated LECs is the cornerstone of the competitive checklist. Yet parity is difficult to achieve when the comparison involves apples and oranges -- the ILEC's self-provision of local exchange service (apples) with its provision of network elements and resale to unaffiliated carriers through a separate, and entirely different, set of operational interfaces (oranges). If the RBOC's retail arm must purchase the same network inputs at the same rates, terms, and conditions as other CLECs, and through the same OSS systems, then those inputs will actually have to work. Parity will be easier to demonstrate (and discrimination will be easier to detect). This principle also requires that when ServeCo purchases local exchange inputs from NetCo, it will do so pursuant to general tariffs, or, if no tariffs exist, under interconnection agreements that are subject to a pick-and-choose requirement.

<sup>37/</sup> As previously noted, this provision must also apply to ServeCo's relationship with HoldCo and all other HoldCo affiliates.

- 4. Substantial public ownership of ServeCo (approximately 40% or more). Under any structure short of full divestiture, HoldCo still will have an incentive to maximize its overall corporate interest through its control of NetCo and ServeCo. However, significant public ownership in ServeCo helps create independent fiduciary duties to shareholders other than HoldCo. This increases the likelihood that ServeCo will compete vigorously in the retail market, price its retail offerings to reflect the actual prices of the inputs it obtains from NetCo, and demand the best prices and quality for network inputs from NetCo. Public ownership also creates disclosure requirements that would make it more obvious if HoldCo were to pursue a strategy of operating ServeCo at a loss while the real profits are made in NetCo (through above cost network input rates to all carriers, for example). Finally, public ownership reduces the return to HoldCo from NetCo misconduct that benefits ServeCo.
- 5. Independent directors on the ServeCo board, including representatives of the non-HoldCo shareholders. Independent directors also will increase the likelihood that ServeCo will act in its own best interests, independent of NetCo and HoldCo. Independent members representing the public shareholders also would serve as "watchdogs" on possible board efforts to put HoldCo interests ahead of ServeCo's independent best interest.
- 6. Compensation for ServeCo management based only on ServeCo performance, not performance of HoldCo or NetCo. Compensation, including bonuses and stock options, that are tied to the performance of ServeCo itself should reduce the incentives of ServeCo management to consider the interests of NetCo in their business plans. Instead, they should demand from NetCo low prices, high network quality, and good service, including access to the most efficient and viable means of providing local exchange service (for example, combined network elements). Broader public benefits then follow because, as noted above, if NetCo provides these efficient inputs to ServeCo, it must also provide them to all other retail service providers.

7. As a key transitional matter, ServeCo would not provide service to a NetCo customer. The retail affiliate (which is also the sole interLATA affiliate of the RBOC) must be required to win the local customer from NetCo before it is allowed to provide interLATA service to that customer. Without this requirement, the RBOC could simply provide interLATA service on a "side-by-side" basis to its existing local exchange customer base without switching a single customer's local service. In these circumstances, the RBOC has little incentive to provide non-discriminatory access to the inputs that non-affiliated CLECs need to provide local service. The conflicts of interest are not really broken. Once a retail local service customer has left NetCo, for example to go to a CLEC other than ServeCo, then ServeCo can be allowed to sell stand-alone interLATA services to such a customer. Once NetCo's operations systems supporting network elements have been shown to be equivalent to the PIC systems used to change long distance carriers, a state commission may then order balloting and allocation to eliminate NetCo's remaining embedded base, and this feature of the plan would expire.

The "seven minimums" LCI identifies are interrelated; each of them must be present to have an acceptable "Fast Track" plan. Again, LCI is not asking the Commission to require structural separation on these terms. And again, states are free to take additional steps beyond the "seven minimums" to reflect their own conditions and statutes, in full accord with their traditional jurisdiction. Thus, the plan in no way alters or affects the jurisdiction of individual PSCs to determine what measures are necessary and desirable to protect local competition and telephone consumers in their state.

But if the "seven minimums" are adopted, we believe that the current stalemate will be broken, consumers (especially residential consumers) can enjoy the benefits of the Act -- and the Commission and the states therefore promptly can grant an RBOC both interLATA entry and

unregulated retail pricing. 38/ This can be seen in the context of the three barriers to local competition discussed above.

## B. Addressing RBOC Conflicts of Interest Will Promote Local Competition.

### 1. Resolution of the OSS Barrier.

Under the "Fast Track" proposal, the RBOC finally will have a direct incentive to design OSS systems of the highest quality possible, as rapidly as possible, because it will have to live with those same systems. In addition, because NetCo must deal with ServeCo as if it were an entirely unaffiliated CLEC, NetCo will be required to create and manage OSS systems and related "customer care" functions that facilitate the retail services of all service providers. 39/ Those systems will function with a single OSS interface used by NetCo to provision ServeCo and all other CLECs. NetCo similarly will be required to give equal treatment to its ServeCo affiliate and other CLECs in such matters as maintenance and customer support. Because the same systems will have to be made available to all CLECs, opportunities to detect discrimination will be greater, reducing the complexity of other Section 251 issues, both pre- and post-Section 271 RBOC entry.

### 2. Resolution of the UNE Barrier.

Under the "Fast Track" plan RBOCs also finally will have an incentive to make available the UNEs needed to provide local service, in the forms needed by competing service providers. Now ServeCo will require UNEs itself, and will have to go to NetCo to get them. In turn, NetCo

<sup>38/</sup> This assumes that the "seven minimums" of the NetCo/ServeCo structure are maintained and enforceable under Section 271(d) on a going forward basis after interLATA entry, subject to the plan's sunset provision. The RBOC would have to agree to this condition.

<sup>39/</sup> The Commission already has held that any RBOC interLATA affiliate must use the same OSS system or "gateway" as unaffiliated CLECs use when ordering local exchange inputs. *Non-Accounting Safeguards Order*, 11 FCC Rcd at 22058, para. 316.

will be required to make UNEs available to all parties on the same terms and conditions.

Unlawful discrimination, if any, should be easier to identify and remedy if it occurs.

LCI believes that this structural approach will have its greatest benefit by bringing competition to residential customers. Mass-market applications such as residential competition require quick, cost-effective and reliable access to network elements. If ServeCo is held to the same ordering and provisions systems as all CLECs, then NetCo will be forced to develop systems which support competition in this sector. Thus, one of the principle advantages of the LCI plan will be widespread local competition to all customer classes, including residential customers.

In short, LCI expects that under its plan RBOC conflicts of interest will be sufficiently reduced to make it much more likely that NetCo will provide UNEs in the form in the form necessary to permit broad-scale local competition to proceed, and do so on efficient terms. In particular, it will be much easier for the Commission to monitor the market, identify any UNE discrimination, and take prompt corrective action. 40/

### 3. Resolution of the Pricing Barrier.

Finally, the LCI "Fast Track" proposal would reduce the competitive risk of unlawful price discrimination. Under the LCI plan ServeCo would see NetCo's charges as real costs -- just like its rivals. ServeCo therefore should have no cost advantage when obtaining UNEs,

<sup>40/</sup> This is not to say that incentives to discriminate with respect to UNEs are eliminated by the LCI plan. Particularly during the early period while NetCo retains the majority of the retail base, HoldCo still will have a strong incentive to discourage use of UNEs. This is because the longer that NetCo retains that base, the longer HoldCo will keep control of the substantial access and other revenues associated with its current retail customers. It would be highly suspicious if ServeCo predominantly offered local service on a Section 251(c)(4) resale basis rather than by making use of UNEs the way that its competitors plan to do. This would suggest that, notwithstanding attempts to make ServeCo independent, HoldCo is still able to profit-maximize by blocking UNE-based competition by retail service providers. This problem will bear watching in the short term. It is why one important element of the "Fast Track" plan is a commitment by the RBOC that NetCo will cooperate in the provision of UNEs in both a combined and uncombined form.

exchange access to embedded base NetCo customers, support activities such as order processing, billing, and maintenance service, or any other wholesale input.

The "Fast Track" plan admittedly has more limited value as a device to encourage NetCo to reduce its rates to economic cost. Over time market forces may help drive down NetCo rates as retail companies — including ServeCo itself — have other network alternatives. It is also expected that ServeCo's non-HoldCo shareholders will exert influence on ServeCo to push NetCo to reduce rates even in the absence of competitive alternatives. However, LCI recognizes that any such pressures will be met by countervailing HoldCo pressures to maximize NetCo revenues for the overall benefit of HoldCo. Therefore, the FCC and state commissions still will need to oversee NetCo's pricing so long as it continues to hold a dominant position in the market for local exchange facilities. As noted above, it remains critical that NetCo comply with the cost-based pricing requirements of the Act. 41/

With that important caveat, local competition can proceed so long as NetCo is strictly prohibited from favoring ServeCo in its pricing (such as through volume or other discounts that only ServeCo can qualify for), and so long as its incentives to do so are mitigated by <u>all</u> the separation requirements discussed above. These plan components, coupled with effective state pricing oversight of NetCo, can permit the FCC to grant a rebuttable presumption of 271 compliance for state-approved prices. Importantly, then, the current stalemate can be broken.

<sup>41/</sup> LCI also recognizes that regulation of NetCo will continue to be necessary to prevent it from blocking the development of competing facilities networks that may eventually erode NetCo's dominance. For example, NetCo still will have incentives to deny reasonable interconnection to other network facilities, whether those of ServeCo or another CLEC. However, the "Fast Track" proposal does nothing to increase this concern, and the inevitable introduction of new facilities by ServeCo should bring beneficial incentives to interconnection in the same way we expect our plan to accelerate retail competition.

Overall, "Fast Track" (i) insulates retail competition from the consequences of excessive NetCo pricing so that it can proceed with minimal regulation, (ii) makes it easier for regulators to identify any anti-competitive conduct by NetCo; and (iii) allows limited regulatory resources to be focused on creating facilities competition that eventually will allow "fast track"-style separation to sunset.

## C. The Electric Utility Industry Analogy

The practical soundness of LCI's proposal is confirmed by significant experience across the nation in other industries. For example, in pursuing restructuring in the electric area (where, as with telephony, the facilities involved in transmission and distribution must be shared by competitors in retail services), state commissions have been motivated by similar concerns with discrimination and lack of competitive choice at the retail level.

Illustratively, in ordering that all electric utilities turn over their control of transmission facilities to an independent entity (the independent system operator or ISO), the California PUC observed, in terms equally applicable here:

The establishment of an ISO lessens the potential for owners of the transmission system to favor their own generation facilities over non-utility facilities in providing transmission access. Coupled with FERC's principles of open, nondiscriminatory transmission access, disaggregation of the transmission function will enhance fair competition among generators. 42/

The California Commission recognized that this structure would generate the "operational efficiency inherent in a transmission network which has no economic interest other than fostering open access and the facilitation of supply from generators irrespective of their ownership." 43/

Likewise in Massachusetts, the Department of Public Utilities concluded that, to minimize the potential for vertical market power abuse by electric utilities, electric companies must functionally separate generation, distribution, and transmission functions, and form separate

<sup>42/</sup> Proposed Policies Governing Restructuring California's Electric Services Industry and Reforming Regulation, California Public Utilities Commission, R. 94-04-031, I.94-04-032, Decision 95-12-063, (Dec. 20, 1995), as modified by D.96-01-099, (Jan. 10, 1996), 166 PUR 4<sup>th</sup> at 18 (also ordering entities selling electric energy to pool their power for sale to others, including "marketers" that sell the power to retail customers) ("California Proposed Policies").

<sup>43/</sup> California Proposed Policies, 166 PUR 4<sup>th</sup> at 18-19 (also noting that this structure would create other lasting benefits, including reduction of disputes, cost savings, and a nondiscriminatory pricing system for use of the common network facilities).

corporate marketing affiliates for all sales of electric power if they retain generation assets. As the Department explained, again in terms applicable here: "[T]hose electric companies that have enjoyed a monopoly position cannot be expected to forgo willingly the advantages that monopoly status afforded them in the past. 44/ The Department concluded that the functional separation of generation from transmission and distribution services was a necessary first step to curb an electric company's ability to provide itself an undue advantage in buying or selling services in competitive markets.

The LCI "Fast Track" proposal builds on these same principles. We recognize that others have suggested that the electric industry model may have lessons for creating local telephone competition. This Commission should take the steps necessary to implement just such a retail/wholesale structure for RBOCs interested in helping break the current stalemate.

### IV. LEGAL AUTHORITY FOR THE PROPOSAL.

The Commission has clear authority under the Communications Act to adopt the declaratory rulings requested here, and thereby clear the path for any RBOC that wants to adopt the "Fast Track" approach. As noted above, LCI is not proposing any change in the substantive requirements of the Act. RBOCs still must comply with Sections 271 and 272 before entering the interLATA market. Section 251 still applies, including the safeguards of Section 251(h) that prevent an ILEC from evading its responsibilities by creating new affiliates. The RBOCs still will be subject to Sections 201 and 202 and other sections of the Act.

In essence, all that "Fast Track" does is create a kind of safe harbor for the RBOCs. The stalemate here is at bottom a question of what are the facts: Have the RBOCs met the essential prerequisites for local competition (the competitive checklist)? Is it in the public interest for them to enter the interLATA market? Is an RBOC evading its Section 251(c) responsibilities by

<sup>44/</sup> Electric Industry Restructuring Plan: Model Rules and Legislative Proposal, Massachusetts D.P.U., D.P.U. 96-100, at 66 (Dec. 30, 1996).

acting through an affiliate or successor? Does the RBOC have market power in a given circumstance such that it must be found a dominant carrier?

The "Fast Track" plan cuts through all of this debate. The Commission would be declaring that -- if the RBOC meets all of the "seven minimums" discussed above -- these factual questions can be resolved quickly in their favor. The Commission does not need to, and should not, take a position on how it might answer these questions on different facts. 45/

LCI submits that establishment of this kind of safe harbor would productively focus on and address the root problem of RBOC conflicts of interest in a comprehensive, integrated fashion. Significantly, RBOCs would in no way be required to take advantage of the safe harbor. They could continue to pursue today's path, and their factual cases would be evaluated under the current regime. 46/ Clearly, however, the Commission has in the past (and would need in the future) to test those facts much more rigorously if the incentives and opportunities to discriminate against competitors are not checked through the "seven minimum" safeguards proposed here.

The "Fast Track" Plan is fully consistent with tools the Commission has used in the past to control anti-competitive conduct. The Commission "has traditionally used its general

<sup>45/</sup> In an important sense, the LCI plan builds on a concept reflected in the Commission's recent *Order* addressing BellSouth's Section 271 application for South Carolina. There the Commission established a "safe harbor" regarding inbound telemarketing scripts to provide guidance to the RBOCs on this narrow but important question. The Commission found that scripts such as the one proposed by BellSouth were acceptable, but made clear that other scripts might or might not be lawful depending upon the facts. *See Application of BellSouth Corp. Pursuant to Section 271*, CC Docket No. 97-208, FCC 97-418, *supra*, at para. 236.

<sup>46/</sup> Those facts, of course, will be influenced by how states require RBOCs to structure their operations. For example, the "Fast Track" plan does not conflict with any authority a state may have to mandate retail/wholesale separation (including separation going further than proposed here) pursuant to its own statutes, and its own review of local market conditions. This Petition only asks the Commission to adopt declaratory rulings to establish a safe harbor, a harbor that the RBOC may enter either voluntarily or pursuant to state direction.

authority under the Communications Act to impose separate affiliate requirements" 47/, and has confirmed its authority to do so since passage of the 1996 Act. 48/

Illustratively, in *Computer II* (which prefigures the Act's Section 272 subsidiary requirements in certain respects), the Commission used its general rulemaking authority to require AT&T (i.e., the integrated Bell system) to offer enhanced services and customer premises equipment through subsidiaries that were separated fully from its telecommunications affiliates. 49/ Similarly, the Commission imposed separate affiliate requirements on independent

<sup>47/</sup> Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services, Implementation of Section 601(d) of the Telecommunications Act of 1996, Report and Order, WT Docket No. 96-162, FCC 97-352, at para. 47 (rel. Oct. 3, 1997) ("CMRS Competitive Safeguards Order"), citing Regulatory & Policy Problems Presented by the Interdependence of Computer & Communications Service and Facilities, 28 FCC 2d 291 (1970) (Tentative Decision) (Requiring common carriers to furnish data processing services only through separate corporate entities meeting certain separation requirements). Policy and Rules Concerning the Furnishing of Customer Premises Equipment, Enhanced Services and Cellular Communications Services by the Bell Operating Companies, 95 FCC 2d 1117 (1983) ("BOC Separation Order"), aff'd sub nom. Illinois Bell Tel. Co. v. FCC, 740 F.2d 465, 467 (7th Cir. 1984) (forbidding the BOCs from offering enhanced services and customer premises equipment other than through separate subsidiaries); Regulatory and Policy Problems Presented by the Interdependence of Computer and Communication Services and Facilities 28 FCC 2d 267 (1971) ("Computer I"), aff'd in part sub nom GTE Serv. Corp. v. FCC, 474 F.2d 724 (2d Cir. 1973).

<sup>48/</sup> See, e.g., Rules and Policies on Foreign Participation in the U.S. Telecommunications Market, Market Energy and Regulation of Foreign-Affiliated Entities, Report and Order and Order on Reconsideration, IB Docket Nos. 97-142, 95-22, FCC 97-398, at paras. 253-55 (rel. Nov. 26, 1997) ("Foreign Carrier Protection Order") (discussing various instances in which the FCC has imposed structural separation requirements on common carriers, and imposing structural separation requirements on U.S. international carriers and their foreign carrier affiliates that possess market power); Bell Operating Company Provision of Out-of-Region Interstate, Interexchange Services, Report and Order, 11 FCC Rcd 18564, 18579, paras. 29, 30 (1996) ("BOC Out-of-Region Provision Order") (offering RBOCs the choice of providing out-of-region, interstate, interexchange services under non-dominant regulation if the RBOCs offer those services through a separate affiliate meeting certain separation requirements, and rejecting arguments that Section 272(a)(2) prohibits the FCC from doing so).

<sup>49/</sup> Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), Final Decision, 77 FCC 2d 384, 486-87 (1980) ("Computer II"), recon., 84

ILECs in connection with their provision of in-region interexchange services, and re-affirmed those requirements after the 1996 Act was passed. 50/ The Commission also has imposed separate affiliate requirements on the LECs' in-region provision of commercial mobile radio services (CMRS), relying on its general rulemaking authority (and no specific statutory provision). 51/ And the Commission recently adopted a requirement that U.S. international carriers regulated as dominant and affiliated with foreign carriers must provide service in the U.S. market through a corporation separate from the foreign carrier affiliate. 52/

The Commission's plenary authority to adopt structural approaches to regulatory problems derives from the Act itself, specifically, from the FCC's statutory power to "make such rules and regulations, and issue such orders, not inconsistent with this Act, as may be necessary

FCC 2d 50 (1980), aff'd sub nom. Computer & Communications Indus. Ass'n v. FCC, 693 F.2d 198, 218-19 (1982) ("CCIA"), cert. denied, 461 U.S. 938 (1983).

- 50/ Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area, Second Report and Order and Third Report and Order, CC Docket Nos. 96-149, 96-61, FCC 97-142 (rel. Apr. 18, 1997), at para. 173 ("Regulatory Treatment Order").
- 51/ CMRS Competitive Safeguards Order, supra, at paras. 4, 47 (requiring ILECs to provide in-region commercial mobile radio service through a structurally separate corporation meeting certain separation requirements, and rejecting arguments that Section 272(a) limits the FCC's authority to impose such requirements).
- 52/ Foreign Carrier Participation Order at para. 257. The Commission's authority to create a regulatory framework specific to a particular corporate structure is not circumscribed by Section 272. Section 272(f)(3) states that "[n]othing in this subsection shall be construed to limit the authority of the Commission under any other section of this Act to prescribe safeguards consistent with the public interest, convenience, and necessity." As the Commission has explained, "Section 272(f)(3) states that [the FCC] maintain[s] authority to impose safeguards under other sections of the Act." CMRS Competitive Safeguards Order at para. 47. Section 601(c)(3) of the Act likewise provides that "the amendments made by this Act shall not be construed to modify, impair, or supersede Federal .... law unless expressly so provided." Thus, while Section 272 prescribes certain requirements concerning affiliates, it does not preclude the Commission from going beyond its minimal terms or from allowing for separate affiliate and related requirements for services and entities other than those listed in that provision. CMRS Competitive Safeguards Order at para. 47; BOC Out-of-Region Provision Order, 11 FCC Rcd at 18579; Regulatory Treatment Order at para. 168.

in the execution of its functions," and to "prescribe such rules and regulations as may be necessary to carry out the provisions of this Act." 53/

All that said, it is important not to lose sight of the central difference between the Commission's actions in these orders, and the declaratory rulings requested here. There the FCC affirmatively mandated private conduct, while under "Fast Track" the FCC is clearing a path without ordering participation. RBOCs can still obtain interLATA authorizations without the presumption contemplated here. In that case, however, the RBOCs' inherent conflicts of interest are likely to make the Section 271 process slower and more complex, and the RBOCs inevitably will have to face more stringent regulation post-entry. LCI hopes the RBOCs will choose the "Fast Track" path. But that is a decision they can make for themselves.

The "Fast Track" option is akin to other recent Commission decisions regarding ILEC regulation. For example, the Commission has allowed ILECs to provide in-region broadband CMRS so long as they do so through a separate CMRS affiliate. 54/ The Commission reached a similar conclusion with respect to RBOC out-of-region interLATA activities, when it stated:

This order, in effect, offers the BOCs a *choice* of providing out-of-region, interstate interexchange services under dominant regulation if they wish to furnish those services directly or under non-dominant regulation if they wish to offer those services through a separate affiliate that meets the separation requirements. 55/

In sum, there is nothing novel about an agency, including the Commission, determining under its rulemaking and regulatory authority that structural separation requirements are

<sup>53/ 47</sup> U.S.C. §§ 154(i), 201(b), respectively; see also 47 U.S.C. § 254(k).

<sup>54/</sup> CMRS Competitive Safeguards Order at para. 4.

<sup>55/</sup> BOC Out-of-Region Provision Order, 11 FCC Rcd at 18579, para. 30; see also Regulatory Treatment Order at para. 173; Competitive Carrier Order, 98 FCC 2d at 1198 (FCC established that it would regulate as non-dominant the provision of domestic, interstate, interexchange services by local exchange carriers if those services were provided through separate affiliates satisfying certain separation requirements).

reasonable means to carry out the intent of a statute to enhance competition. This petition seeks far milder steps that are squarely within the scope of the Commission's authority.

#### V. OVERALL BENEFITS OF THE "FAST TRACK" PLAN.

The proposal promises numerous benefits for all concerned, including consumers, RBOCs, CLECs, this Commission and the states. We have discussed these benefits in the context of the three barriers of OSS, UNEs and pricing. But stepping back, the overall benefits of "Fast Track" are compelling:

# A. Faster Advent of Local Competition, Especially Residential Choice.

The proposal could be adopted and implemented quickly, with open, residential retail competition beginning by the end of 1998. Doing so promises to allow for a far quicker opening of local telephone markets than otherwise likely will occur, as well as entry of the RBOCs into the long distance market more quickly.

In particular, "Fast Track" will establish retail competition in the residential market, where the RBOC's dominant network position is today most complete, and where it is otherwise likely to continue for the foreseeable future.

## B. Simplification of Section 271 Compliance.

The proposal provides a far simpler and faster way for any RBOC to meet Section 271. It also would make the Commission's Section 271 review work simpler, and should eliminate much of the dispute now taking place in Section 271 proceedings. This is not a trivial matter. LCI believes its proposal will streamline the 271 process as the RBOC incentives shift from demonstrating theoretical or nominal compliance to achieving actual compliance, for the benefit of ServeCo -- and all other CLECs.

## C. Reduced Need for Regulation With Enhanced Post-Entry Competition.

The RBOC conflicts of interest discussed in this petition not only delay retail competition, they also require significant regulatory intervention. Some of that can be seen in

the initial involvement of federal and state officials in complex technical questions regarding how the local network can be opened up in the first place. But even after interLATA entry occurs, ongoing regulation will be necessary to check the continuing incentives of the RBOCs to favor their own retail services. Such regulation will be difficult, costly, and burdensome. Adoption of LCI's "Fast Track" proposal would not eliminate the need for all such regulation and supervision, but it would reduce it substantially because the new corporate structure would reduce both the incentives and the ability of NetCo to discriminate.

Importantly, while many difficult regulatory problems would be simplified under "Fast Track", none would become more difficult. States and the FCC still will face questions regarding such matters as the costing of network facilities, recovery of RBOC historical costs, the appropriate level of universal service support, and network quality and reliability. But in each case, separation of the RBOC's retail services in this fashion allows regulatory attention to focus on NetCo, the remaining dominant firm. The retail market can be substantially deregulated.

In short, the proposal would provide ongoing assurance after interLATA entry that, under the Department of Justice's test, the process of opening the local telephone markets to competition is in fact "irreversible" because the new incentive structure for the BOCs will promote ongoing compliance with the Act. 56/

## D. Promotion of Universal Service.

The "Fast Track" Plan also simplifies the process of protecting universal service goals. First of all, the plan is consistent with current universal service rules. To the extent that NetCo continues to serve the embedded retail customer base of the RBOC, it will qualify for universal service in appropriate circumstances. Similarly, ServeCo will be eligible for universal service on the same basis as other CLECs.

<sup>56/</sup> See DOJ Ameritech Michigan Evaluation at 3.

But beyond that, the process of promoting universal service should become easier under the plan. As a threshold observation, the first key to achieving universal service is achieving universal competition. In an environment of robust competition for residential customers, the principle concern of universal service (that rates will be unaffordable) is lessened. Competition by definition should exert downward pricing pressure. Second, once NetCo is out of the retail market all together, it will be compensated directly and fully for the cost of its wholesale inputs and service activity. It will not receive universal service, nor will it pay universal service contribution because it will not be serving end users. NetCo pricing issues thus will not need to be complicated by this issue, and can focus only on ensuring recovery of NetCo's actual costs.

The universal service policy issue will then focus entirely where Section 254 intended: on how much revenue is needed to meet universal service goals, and how to ensure that this revenue is distributed on a competitively neutral basis to ServeCo and all other firms providing retail services qualifying for support. Regulators will have a much easier time addressing these issues -- and ensuring the competitively neutral administration required by the Act -- under the Fast Track Plan.

## E. Enhanced Maintenance of Network Quality and Reliability.

"Fast Track" will give NetCo strong incentives to maintain network quality and reliability because over time it will have as its sole focus its carrier's-carrier function, with an unmixed incentive to make it as feasible and efficient as possible to use its wholesale facilities and operation systems. To the extent price increases are necessary to pay for such enhancements, the state commissions can assess and perform this function just as they do now—but in far less contentious circumstances. Over time the arrival of competing networks should reduce the need for regulation in this area.

At the same time, it is significant that "Fast Track" in no way restricts the ability of ServeCo to build its own facilities (as opposed to have facilities assigned to it at separation). Once ServeCo is properly established, it may build whatever facilities it wants free from the

obligations of Section 251(c) to make those facilities available to other carriers. Thus, the plan responds to complaints by some RBOCs -- unjustified in LCI's view -- that the current structure deters investment and innovation.

#### F. AIN.

The proposed NetCo/ServeCo structure also would produce benefits in connection with the Advanced Intelligent Network (AIN). NetCo would have improved incentives to provide open access to AIN components, such as the Service Control Point, Service Creation Environment, and Service Management System, in order to meet the needs of carrier customers. NetCo would have more incentive to ensure that the interfaces to each system were well documented and easy to use, and to provide for fully automated provisioning. If, on the other hand, NetCo were to require competitors to access the signaling network (and hence switch triggers) via a mediation point, then ServeCo would be required to do so as well. Thus, network reliability issues and competitive equality will be addressed because ServeCo and its CLEC competitors will be on an equal footing as regards NetCo's AIN. "Fast Track" is likely to accelerate deployment of enhanced AIN services by all service providers, with huge benefits for American consumers. But at a minimum, the RBOCs at least could no longer discriminate against competitors regarding access to AIN capabilities.

#### VI. THE ROLE OF STATE COMMISSIONS.

LCI fully recognizes the central responsibility of state commissions to regulate local markets. The state commissions bear front line responsibility for ensuring that every American enjoys the benefits of local telecommunications competition. InterLATA entry also will be a watershed event for the states, presenting new issues and challenges.

"Fast Track" responds to these intrastate developments and recognizes the key role and unique perspective of the states. That is why LCI is filing related petitions with both the Illinois

Commerce Commission and the New York Public Service Commission, and welcomes consideration from other states.

The ICC and NYPSC petitions will ask those Commissions to open proceedings: (a) to consider the intrastate actions necessary to implement "Fast Track," and (b) to investigate more generally how RBOC interLATA entry will impact, and necessitate modification of, each state commission's existing regulatory requirements. LCI is filing in these two states because they were among the first to begin efforts to create local competition nearly a decade ago. Thus, the importance of eliminating the continuing barriers, so that competition can extend broadly to residential and small business customers, is most apparent in these states with their long history of attempting to open the market. The NYPSC also has the benefit of its experience with the separation of Rochester Telephone. LCI recognizes that other states have been very active in trying to foster local competition as well. "Fast Track" is designed to work throughout the nation.

If the RBOCs are to enter the interLATA market, states will obviously need to consider how that entry may require revision of existing regulations. This is true however RBOCs structure their business operations. However, LCI submits that its "Fast Track" plan is directly relevant to such inquiries into post-271 intrastate regulation. If RBOCs adopt the structural separation proposed here (and such other measures as a particular state commission might deem necessary) then it would be appropriate for states to grant ServeCo substantial flexibility in the pricing of its retail services -- flexibility equivalent to that afforded to other CLECs. Conversely, however, if the interests of the RBOC wholesale and retail operations remain intermixed, then interLATA entry will need to be accompanied by new regulatory oversight to make sure that the RBOC does not discriminate in favor of itself with respect to exchange access, UNEs and other wholesale inputs. Bundled pricing of retail services (combining local, toll, and other services) will make it more difficult to detect cross-subsidization and to enforce imputation requirements, for example.

In short, "Fast Track" in no way alters or amends existing state authority and jurisdiction. State commissions would have to approve any restructuring plans, adjusting details if necessary to fit their unique statutory authority, established practices, and local conditions. 57/ Specific state actions would include: (i) modifying today's price-cap/incentive regulatory plans to reflect the separation of the RBOC's wholesale/retail roles and the reduced regulation of ServeCo's retail offerings; (ii) adopting transitional requirements to ensure that basic local service will continue to be available under the terms of existing price-cap/incentive mechanisms; and (iii) verification, with the FCC, that the prerequisites of the new structure have been implemented.

Thereafter state commissions would continue to have the primary responsibility for pricing of NetCo's carrier's-carrier (and residual local exchange service) offerings, as well as the intrastate retail and access services provided by ServeCo. 58/ LCI fundamentally expects that less regulation will be needed under its plan because residential customers will be courted by many service providers, not just one. But the bottom line is that the plan does nothing to limit the states' ability to regulate their telecommunications markets -- it only reduces RBOC conflicts of interest so that a state commission's job is made easier, both today and in the post-271 future.

### VII. OTHER ISSUES ADDRESSED BY THE PROPOSAL.

### A. Protecting the Integrity of the Network.

As noted above, NetCo should have every incentive to continue making investments to preserve its network integrity. TELRIC-based UNE rates should include compensation for this

<sup>57/</sup> Of course, the RBOCs still would have to meet the "seven minimums" upon which the proposed declaratory rulings rest in order to qualify for "Fast Track" treatment.

<sup>58/</sup> LCI's proposal contemplates that a state commission would substantially eliminate regulation of the prices for ServeCo's retail and exchange access services upon implementation of this plan, but of course the state would retain jurisdiction over these and any competing retail CLEC services as necessary to protect basic service or any other policy.

obligation, and NetCo's customers, including ServeCo and the CLECs, will demand a high quality standard. Moreover, current FCC and state regulatory mechanisms to monitor network quality and investment would continue to apply to NetCo. In addition, the development over time of competitive networks should provide NetCo an increasingly strong incentive to keep its network attractive to service providers, whether ServeCo or other CLECs, through additional fiber optic cable, upgraded switches, AIN deployment, and other investments in new technology. Finally, our related state petitions include transitional mechanisms, based on existing price-cap incentives, to assure the continued availability of a basic local exchange service comparable to that offered today.

## B. Status of ServeCo as an ILEC Under Section 251(h).

In this petition, LCI has asked the Commission to declare that any RBOC adopting the proposed corporate structure may offer local exchange service through its retail affiliate without concern about being classified as an incumbent LEC under Section 251(h). 59/ Incumbent LECs have begun to seek authority from commissions in a number of states to create a "CLEC affiliate" through which they intend to offer local exchange service in competition with themselves, in their own service areas. State commissions have struggled with the notion that the ILEC could create another company to provide local exchange service that would be free from the requirements of Sections 251(c) and 252. 60/ The FCC also may soon be asked to resolve the

<sup>59/</sup> Section 251(h)(1)(B)(ii) of the 1996 Act provides that any "successor or assign" of an incumbent LEC also must be treated as an incumbent LEC. 47 U.S.C. §§ 251(h)(1)(B)(ii). Section 251(h)(2) allows the FCC to classify as an incumbent LEC any LEC that occupies a position in the local market "comparable to" the position held by an incumbent LEC and has "substantially replaced" an incumbent LEC. 47 U.S.C. § 251(h)(2). Whether an entity should be treated as an ILEC is for the Commission to decide.

<sup>60/</sup> The Texas Commission, for example, has denied GTE a CLEC certificate in its own service area because of these concerns. See GTE CLEC Certification Order, supra ("The service area of GTE-CC's COA is limited to the service area of SWBT, Sprint/United, and Centel").

legal and factual question whether the CLEC affiliate of an ILEC should be considered an ILEC under Section 251(h). 61/

An RBOC can avoid the danger of having its interLATA affiliate regulated as an ILEC when it provides local exchange service out of that affiliate by adopting the NetCo/ServeCo structure. Under that structure, the ILEC's Section 251(c) interconnection responsibilities will be met by NetCo, who will have the network facilities to fulfill that role -- and now the reduced conflicts of interest to help it do so on a nondiscriminatory basis.

If LCI's proposal is adopted, the Commission also should rule that ServeCo is not a "successor" or "assign" of the RBOC, and that ServeCo does not occupy a comparable position in the local exchange market, because ServeCo is adequately separated from NetCo and has not assumed the embedded customer base. 62/ Consequently, any RBOC adopting LCI's proposed ServeCo/NetCo structure would not be considered an incumbent LEC within the meaning of

Some might argue that the FCC already has decided that an RBOC's interLATA affiliate 61/ cannot become an ILEC under Section 251(h) when it offers local exchange service from the affiliate. This would be incorrect. It is true that the Commission concluded in the Non-Accounting Safeguards proceeding that an RBOC's Section 272 affiliate may provide local service as well as long distance service out of that affiliate. Non-Accounting Safeguards Order, 11 FCC Rcd at 22055-56, para. 312. The FCC also held that the mere fact of providing local exchange service in and of itself does not make the affiliate an incumbent LEC within the meaning of Section 251(h). Id. The FCC did not determine, however, at what point a transfer of the local exchange functions or customers to the affiliate might trigger a finding that the affiliate should be treated as an ILEC within the meaning of Section 251(h). In fact, the FCC effectively begged the question in the Non-Accounting Safeguards Order, by stating only that the interLATA affiliate may offer local exchange service provided it does not qualify as an ILEC within the meaning of Section 251(h). Id. (emphasis added). Thus, the FCC has correctly left open the question of under what factual circumstances an ILEC affiliate that is providing local exchange service would become an ILEC itself under Section 251(h).

<sup>62/ 47</sup> U.S.C. § 251(h)(1), (2). We note, however, that the Commission already has held that if an RBOC were to transfer any of its local exchange facilities to its interLATA affiliate, the affiliate would become an incumbent LEC under Section 251(h)(1) with respect to those facilities. Non-Accounting Safeguards Order, 11 FCC Rcd at 22054, para. 309. In any case, we propose in this plan that NetCo be prohibited from transferring network facilities or existing customers to ServeCo, because such transfer would be inconsistent with NetCo's role as carrier's-carrier to the retail operations of ServeCo and others.

Section 251(h). 63/ This would assure RBOCs that their ServeCo affiliates, like other CLECs, would not have to offer the interconnection features mandated under Section 251(c), regardless of the extent to which they are themselves offering local exchange service. 64/

# C. Regulation of ServeCo Interstate Services.

One of the premises of LCI's structural approach is that the ServeCo affiliate would be deregulated in all material respects, and would enjoy the same non-dominant carrier status that its competitors have, as it enters the local, intraLATA and interLATA markets. This would ensure that the RBOC can compete on a retail level on an unrestrained, deregulated basis. 65/

Today RBOC interLATA affiliates are subject to more stringent regulation than other service providers in several important respects. For example, such affiliates today would be treated as dominant when they offer bundled packages of local exchange and interLATA (and other) services. 66/ This is appropriate, given that the RBOCs have demonstrated the ability to discriminate in favor of their own local services, and that competitive problems in the local market all the more infect the interLATA market when local and long distance services are sold together in a bundled form.

Moreover, under current regulatory decisions and current case law, although the Commission previously has decided that the stand-alone in-region interstate interLATA services

<sup>63/</sup> Of course, the Commission would retain discretion to classify a ServeCo as an ILEC if over time, the NetCo/ServeCo structure does not function as we predict it will.

<sup>64/</sup> The end point of our proposal contemplates that NetCo no longer will have retail local exchange customers, and that the RBOC will provide local exchange service only through ServeCo in competition with other CLECs.

<sup>65/</sup> We recognize that some of the necessary deregulatory steps (for intrastate services) must be taken at the state level.

<sup>66/</sup> The Commission has not yet addressed the regulatory treatment of RBOC bundled offerings, which therefore remain classified as dominant. See Regulatory Treatment Order at paras. 85-92. By "bundled" offerings, we mean selling both local and long distance at a single price, so that it is not possible to determine what the separate price for each service might be.

of a Section 272 affiliate should be treated as non-dominant, that decision rests on a foundation that is no longer valid. Specifically, the Commission's order relied in significant part on full implementation of its *Local Competition Order*, including those parts of the *Order* most necessary to permit RBOC competitors to use cost-based and efficiently provisioned UNEs in place of RBOC exchange access. However, key components of the *Local Competition Order* subsequently were invalidated by the Eighth Circuit, thereby invalidating the foundation for the Commission's previous ruling regarding regulation of RBOC interLATA services. 67/ Thus, an essential underpinning of the Commission's non-dominance decision is now missing, and the Commission will need to re-evaluate and reverse its decision accordingly. 68/

For RBOCs that opt to implement the "Fast Track" structure, however, the Commission reasonably can, and should, declare that the ServeCo retail affiliate would be treated as a non-dominant carrier with respect to all its interstate retail offerings, including bundled packages that include local as well as interstate services. Dominant carrier regulation—which is primarily designed to prevent unreasonable discrimination, cross-subsidization, and other anti-competitive conduct—would be unnecessary if an RBOC were to adopt LCI's proposed structure. This is an additional important simplification of post-271 regulatory oversight for any RBOC which adopts LCI's "Fast Track" plan.

<sup>67/</sup> See e.g., Iowa Utilities Board v. FCC, (Oct. 14, 1997 Order) (invalidating 47 C.F.R. § 51.315(b)); Iowa Utilities Board v. FCC, 120 F.3d 753, 793-800 (invalidating FCC's adoption of TELRIC providing standard for UNEs).

<sup>68/</sup> For example, if the RBOC's interLATA affiliate purchases network elements from the RBOC to provide local exchange service, it may not be pricing that local service to cover the cost of the UNEs. In the absence of an independent fiduciary obligation in the affiliate, the affiliate is indifferent as to whether it covers the cost of inputs obtained from NetCo. In contrast, the ServeCo structure enhances prospects that ServeCo would accurately reflect the prices of inputs obtained from NetCo in its retail prices, and to insist that NetCo sell it inputs at cost, not at artificially inflated prices. As we also discussed above, the fact that the RBOC must charge the interLATA affiliate the same thing the RBOC charges others does not mean that those prices are real from the affiliate's point of view. See, e.g., 47 U.S.C. § 272(e)(3).

At the current time any exchange access services provided by an RBOC Section 272 affiliate still are considered dominant and regulated accordingly. This is appropriate given the regulatory problems discussed above. However, if the proposed ServeCo structure is adopted, the Commission can safely treat ServeCo's exchange access services as it would any other CLEC's. The Commission has declared that CLECs are non-dominant in their provision of exchange access, and has forborne from requiring CLECs to file tariffs for interstate exchange access. 69/ Under the corporate structure we propose, it is appropriate to treat ServeCo in the same fashion.

# CONCLUSION AND RULINGS REQUESTED

For the reasons set forth above, the Commission should issue the following declaratory rulings that would apply if an RBOC structures its operations so as to establish an independent "ServeCo" and otherwise comply with the conditions of LCI's "Fast Track" plan:

- 1. Section 271 and 272. When such RBOC submits an otherwise acceptable application for authorization to provide interLATA services originating in any in-region state, the RBOC shall receive a rebuttable presumption that it has met the competitive checklist provisions of Section 271(c)(2)(B) of the Act; that provision of interLATA service on this basis meets the requirements of Section 272 of the Act; and that the requested authorization is consistent with the public interest, convenience and necessity.
- 2. Section 251(h). A "ServeCo" created thereunder shall not be deemed a "successor or assign" of an ILEC for purposes of Section 251(h)(1)(B)(ii) of the Act, nor shall it be deemed a "comparable carrier" to an ILEC for purposes of Section 251(h)(2).
- 3. <u>ServeCo Regulation</u>. A "ServeCo" created thereunder shall be deemed a non-dominant carrier to the same extent as a CLEC that is not affiliated with an RBOC.

<sup>69/</sup> See Access Charge Reform Order at paras. 359-64; Hyperion Telecommunications, Inc. Petition Requesting Forbearance, Memorandum Opinion and Order and Notice of Proposed Rulemaking, CCB/CPD Nos. 96-3 & 96-7 and CC Docket No. 97-146, 12 FCC Rcd 8596 (1997).

LCI urges the Commission to act expeditiously to grant these rulings, working with the relevant state commissions considering these matters, so that the current stalemate regarding local competition can be broken, with the benefits of full, robust competition for residential consumers.

Respectfully submitted,

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